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1 INTRODUCTION

After global economic activity declined by 0.6% in 2009, primarily as a result of the continuing recession in developed economies, 2010 saw a recovery in activity and trade. GDP growth was particularly pronounced in developing countries. The moderate economic growth in developed economies was primarily the result of import demand from emerging economies, government stimulus measures and liquidity support by central banks.

Slovenia's economic growth of 1.2% in 2010 was less than the euro area average, primarily as a result of the deepening crisis in construction and adverse developments in financial intermediation. Growth in domestic demand, ignoring the renewal of inventories, remained negative, primarily as a result of the continuing decline in investment, while growth in private consumption was barely positive. Net exports accounted for just over two-thirds of overall GDP growth, primarily as a result of orders from Slovenia's main trading partners. As a result of the adverse situation on the labour market and public finance consolidation, the majority of economic growth will remain based on exports, as a result of which maintaining the right macroeconomic policies to ensure price and cost competitiveness is of key importance to Slovenia's economic performance.

Average inflation as measured by the HICP stood at 2.1% in 2010, up 1.2 percentage points on 2009, and 0.5 percentage points more than the euro area average. The largest contributions to the increase came from energy prices and higher excise duties. As a result of the weak recovery in activity and demand, core inflation remained low, which could prove to be merely temporary as a result of adverse movements in input costs. Growth in unit labour costs slowed in 2010, which can be attributed to the effect of an increase in productivity as a result of a fall in employment. The trends over the medium term nevertheless show these costs to have risen by more than in the majority of euro area countries.

The most notable features of the Slovenian banks' operations last year were the decline in total assets and their overall operating loss. Given the adverse situation on the financial markets, the banks made debt repayments to banks in the rest of the world, and repaid the liabilities to the Eurosystem that had increased sharply the previous year, while the government reduced its deposits at banks, and households recorded a modest increase in deposits. The banks adapted by reducing investments in securities and investments at banks. At the same time, by curbing growth in lending to corporates they continued to respond to the growing problems in the corporate sector, where recapitalisations have for several years failed to improve the poor ratio of equity to debt financing. The cumulative problems faced by the corporate sector showed themselves in two ways last year. First, the gap between credit demand and creditworthy demand widened, and second, there was a large increase in arrears and in non-settlement of financial liabilities, including those to banks. The deterioration in the quality of the credit portfolio and the resulting unavoidable increase in impairment and provisioning costs were the main reasons for the banking system's losses last year. The banks' business with households was satisfactory. It expanded, primarily as a result of long-term housing loans.

Despite the prominent credit risk and income risk, the banking system maintained adequate liquidity and solvency last year. Given the need for the banks to take a more active role in finding a way out of the crisis, the recapitalisation of certain banks will be vital in 2011.

Ljubljana, April 2011

Marko Kranjec
Governor of the Bank of Slovenia

1.1 Implementation of the Bank of Slovenia's strategy

Last year was the second year of the implementation of the Strategic Plan for 2009 to 2012. In the plan the Bank of Slovenia defined seven core objectives that it would pursue in its activities.

Core objective I: „To ensure price stability in the euro area by participating in the definition and implementation of the Eurosystem's monetary policy"

The Eurosystem responded properly to the economic situation by adjusting interest rates. As a result of the economic crisis it had also introduced non-standard instruments into monetary policy, which it began gradually withdrawing in 2010 with the normalisation of the situation. The Bank of Slovenia continued to actively pursue monetary policy via non-standard Eurosystem measures in 2010.

Core objective II: „To support general economic policy to achieve social welfare in the Republic of Slovenia"

In regular publications of economic and financial developments the Bank of Slovenia constantly assessed the macroeconomic and financial trends in Slovenia, and in the Price Stability Report it reported its forecasts of these trends twice a year, together with an assessment of uncertainties in the economic environment. Within the framework of the standard methodology it helped to frame the Eurosystem view of the public finance developments in Eurosystem countries, and regularly participated in the formulation of the Eurosystem's macroeconomic forecasts. It encouraged independent analysis and research, and provided databases for analytical and model assessments to support the guidance of economic policy. In 2010 the Bank of Slovenia began a project on standard reporting for insurance corporations together with the Insurance Supervision Agency (ISA) and the Slovenian Insurance Association (SIA), based on the matrix reporting system for banks (introduced in 2006) and investment funds (developed in 2009). Within the ESCB and the CEBS it participated in the coordination of the methodology for monetary and financial statistics for the needs of supervision. The Bank of Slovenia met its statistical reporting obligations in the Eurosystem with the requisite quality, and ensured public access to data in accordance with the statistical standards of the ESCB and the European Statistical System (ESS).

Core objective III: „To strive for financial stability, the quality supply of cash and secure and effective payment systems, taking into account the principles of market economy, free competition and the interests of consumers"

The Bank of Slovenia analyses the stability of the Slovenian financial system. In addition to conducting periodic internal analysis, it draws up a comprehensive analysis of the changes in risk in the banking system and an analysis of the stability of the financial system twice a year. The analysis is published, and appropriate measures are taken in response to the identified changes where the need arises. The Bank of Slovenia participates in the Eurosystem to determine demand for cash and, within a narrower group of national central banks, on the basis of an agreement to print banknotes, it commissions the printing of the allocated quantity of banknotes on the basis of a public tender. It ensures that there are no disruptions in the supply of banknotes via five depot banks, recirculating the acceptable banknotes and withdrawing the unacceptable ones. Together with other national central banks and the ECB, the Bank of Slovenia participates in the projects and activities by which the Eurosystem implements the process of integrating, harmonising and standardising payment and settlement systems in the euro area (T2S, CCBM2, SEPA), and ensures that they operate smoothly. By reviewing the functioning of payment systems it assesses operational risks, and requires operators and participants to manage these risks appropriately.

Core objective IV: „To optimise the Bank of Slovenia's active role in the ESCB through specialised activities"

The Bank of Slovenia regularly participates in the activities of the ESCB's committees, and directs the activities of its committee members. It requires the relevant staff to assess details and the positions regarding proposals discussed by the Governing Council of the ECB. It also adjusted its internal organisation of work to the working methods of the ESCB. In conjunction with the Austrian and Italian central banks and the ECB, the Bank of Slovenia was actively involved in the preparation and execution of the Financial Information System project in 2010, the aim of which is to introduce standardised information solutions for reporting transactions between central banks in the Eurosystem. The Bank of Slovenia also participates in joint Eurosystem programmes to provide technical assistance, itself designing a programme of bilateral technical assistance aimed at central banks in countries of the western Balkans that are not yet EU Member States. It also participates actively in the programme of the Centre of Excellence in Finance, which operates under the sponsorship of international financial institutions.

Core objective V: „To shape and introduce conditions for a stable and efficient banking system and for the security of deposits at banks and savings banks"

Banking supervision is based on the effective implementation of banking directives and other relevant directives, which are being relatively rapidly updated and amended as a result of the financial turmoil. In 2010 the Bank of Slovenia actively participated in the drafting of national legislation and regulations governing the operations of banks and savings banks. Here the deposit guarantee scheme was of particular importance in 2010. By actively monitoring the effects of the anti-crisis measures and recommendations, and by supervising credit risk, the Bank of Slovenia continued to encourage an appropriate response from senior management at the banks to the difficult business conditions inside and outside Slovenia. Only in this way were the banks able to take up any increased credit risk, and to adequately ensure their liquidity.

Core objective VI: „To ensure a reliable system of risk management system and business continuity processes"

The Bank of Slovenia sets out risk management policy and supervises the implementation of the policy via two channels: financial risks via the Investment Committee, and operational risks, information system security and business continuity via the Operational Risk Committee. In both fields it is developing new methods and gradually introducing them into practice to improve risk management, thereby mitigating the risks to which it is exposed. In 2010 the Bank of Slovenia set up a new backup computer centre, and put into practice a higher level of reliability in the business continuity system.

Core objective VII: „To ensure and support an effective, flexible and cost-effective organisation with motivated and professionally qualified employees"

In 2010 the Bank of Slovenia again reduced its operating costs relative to the previous year, by 3.4%. The effective number of employees remains below the target level set by the financial plan (428). At the same time the average qualifications of the workforce are improving. The Bank of Slovenia is gradually operationalising medium-term planning, the cost monitoring system for central bank functions, project work and the computerisation of development work.

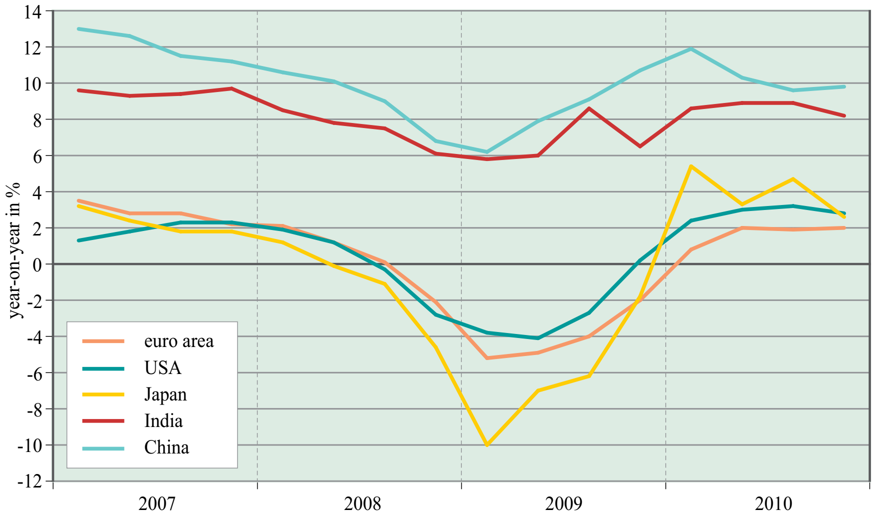
1.2 The economic environment and the banking system in 2010[1]

Economic environment

2010 saw a gradual recovery in developed economies and rapid growth in emerging markets.

After global economic activity declined by 0.6% in 2009, primarily as a result of the continuing recession in developed economies, 2010 saw a recovery in economic activity. GDP growth was particularly pronounced in developing countries. The moderate economic growth in wealthier economies was primarily the result of state aid and central bank stimulus measures, and rapid growth in import demand from developing countries. In 2010 these were already recording their pre-crisis levels of growth. According to initial IMF estimates, global GDP increased by 5.0% in 2010, the BRIC[2] countries accounting for a large proportion of overall growth. Their share of global GDP is now almost 25%. Economic growth in 2010 exceeded 10% in China, and approached 9% in India. The rapid growth in activity also increased inflationary expectations, for which reason the central banks in the two countries began pursuing a restrictive monetary policy at the end of 2010. In the developed economies economic growth in 2010 was moderate in the euro area at 1.7%, but rose to 2.8% in the US.

Figure 1: **GDP growth in selected major economies**



Note: Figures for the euro area, US and Japan are adjusted for the season and the number of working days
Sources: Eurostat, www.tradingeconomics.com (China, India)

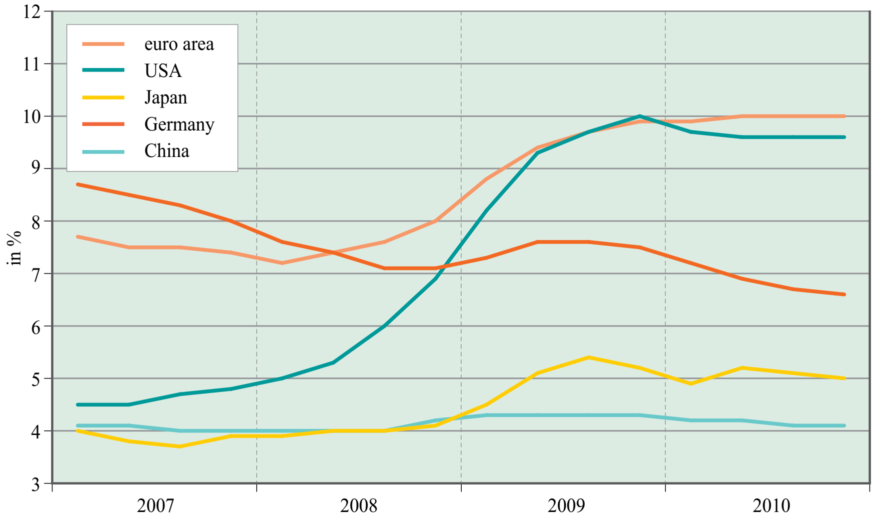
Increased state aid to the economy and lower tax revenues led to increased budget deficits and public debt in developed countries.

The increased state aid to the economy and lower tax revenues led to significant increases in the budget deficit and public debt in developed economies. This also brought downgradings of sovereign debt and banks in the euro area periphery countries, and a rise of yield spreads of their bonds, Greece and Ireland in particular, over the lowest-risk bonds. This further increased the urgency of fiscal consolidation in the euro area countries. As a result of the increase in public debt and problems with servicing their large general government deficits, Greece and Ireland asked the EU for financial assistance, in April and November 2010 respectively. Together

1 A detailed illustration of macroeconomic trends and projections is given in the April 2011 Price Stability Report. Detailed analysis of the banking system is given in the May 2011 Financial Stability Review (http://www.bsi.si/en/publications.asp?MapaId=712).
2 Brazil, Russia, India and China.

with the IMF, the EU provided funds to stabilise the situation on the government bond markets. Last year's inadequate economic growth was also reflected on the labour markets in the euro area and the US, in the low number of new hires and the persistence of unemployment between 9% and 10%.

Figure 2: **Unemployment rates in selected major economies**



Note: Seasonally adjusted quarterly unemployment rate for euro area, US, Japan and Germany
Sources: Eurostat, www.tradingeconomics.com (China)

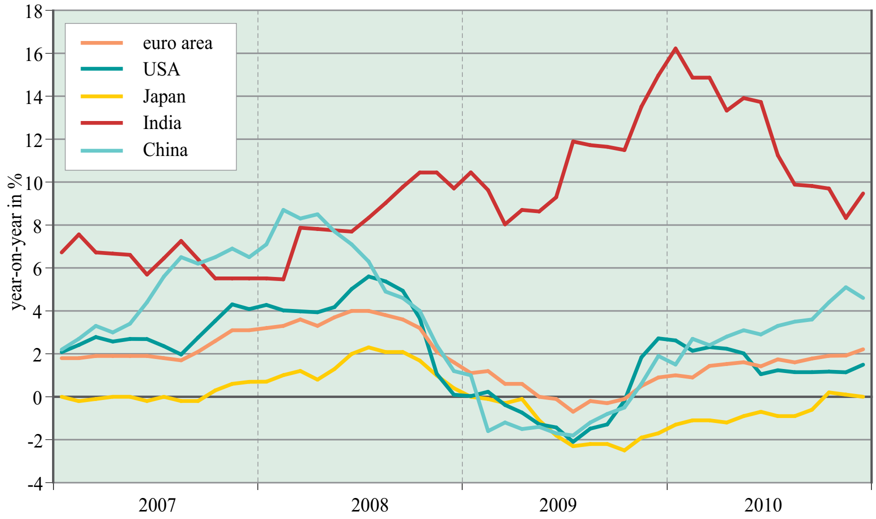
Inflation in developed economies was low in 2010, primarily as a result of the relatively low level of domestic household consumption …

… but inflationary pressures strengthened at the end of the year as a result of growth in commodity prices.

Inflation in developed economies was low in 2010, primarily as a result of the relatively low level of domestic household consumption. This was reflected in low core inflation, which in 2010 stood at 0.9% in the euro area and 1.0% in the US.[3] Inflation as measured by overall growth in consumer prices also remained low on average over the year. In 2010 it stood at 1.6% in the euro area and the US, while prices in Japan fell by 0.7%. Under the influence of high economic growth, inflation rose in China, and in India it stood at over 9%, despite a gradual fall. As a result of faster growth in commodity prices and the rapid economic growth, the central banks in the two countries began pursuing a more restrictive monetary policy in the final quarter of 2010. The rapid growth in commodity prices meant that price pressures had begun to be expressed in price growth in the euro area and the US by the end of 2010. The fall in the euro was another factor in the faster pass-through of US dollar commodity prices into euro area inflation.

[3] The HICP excluding energy and unprocessed food for the euro area; the consumer price index excluding energy and food for the US.

Figure 3: **International comparison of consumer price indices**

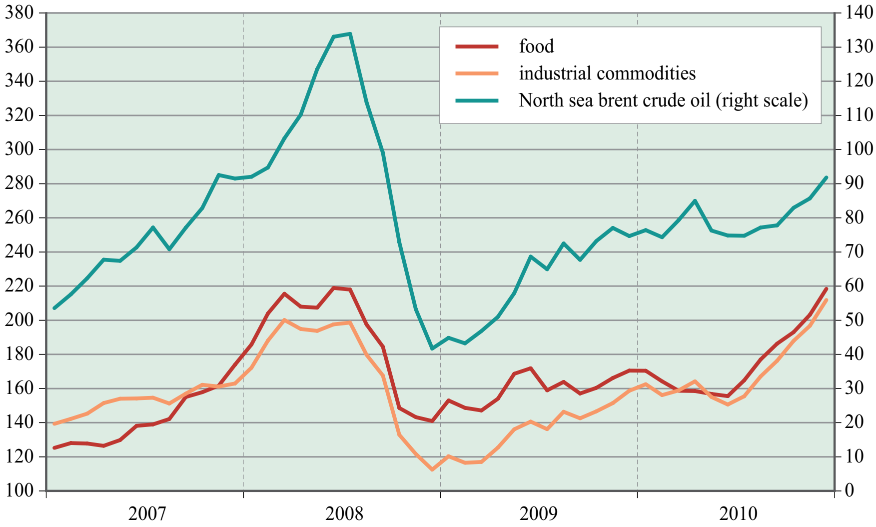


Sources: Eurostat (euro area), Bureau of Labor Statistics (US), www.tradingeconomics.com (India, China, Japan)

Growth in oil and commodity prices was moderate in the first half of 2010, but increased sharply in the second half of the year.

Growth in commodity prices and oil prices was moderate in the first half of 2010 as a result of the uncertain recovery in developed economies, but increased sharply in the second half of the year under the influence of increased demand from emerging economies and higher forecasts of GDP growth for the US in 2011. A barrel of Brent crude averaged USD 80 in 2010, up 29% on the previous year's average. The euro's fall against the US dollar meant that the euro price was up 36%. The price of a barrel exceeded USD 90 in December 2010, which was the level in early 2008, when the extremely rapid growth in oil prices and other commodity prices began. Average prices of primary commodities were up 25% on 2009, prices of industrial commodities recording the largest increase, of 47%. Food prices were up just under a tenth, growth increasing at the end of the year in particular, reaching 28% in year-on-year terms in December. The rise in food prices was primarily the result of adverse weather and higher demand from developing countries.

Figure 4: **Prices of commodities and oil on the global market**

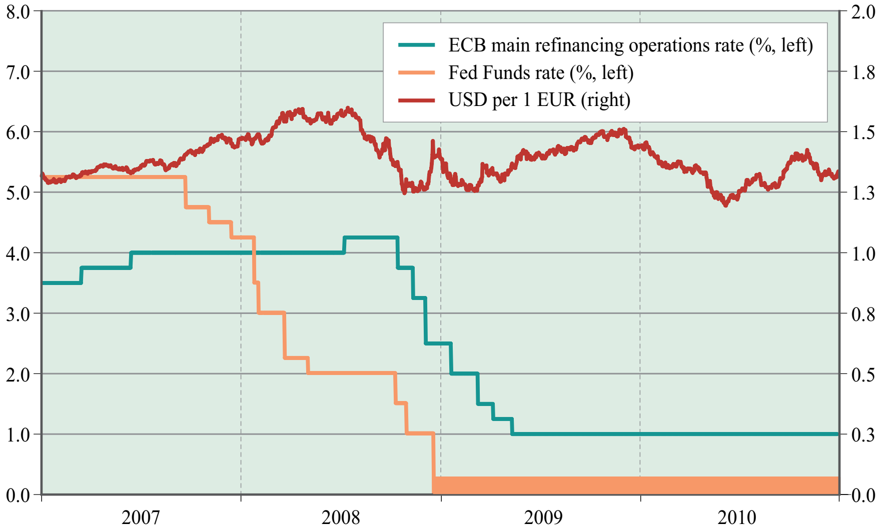


Note: Index 2000 = 100; oil: price of Brent crude, USD per barrel
Sources: The Economist, London; Bloomberg

In the larger developed economies, central bank policy remained stimulative in 2010, but in developing countries the central banks have already begun to raise their key interest rates.

Central bank policy in the major developed economies remained stimulative in 2010, while in the major developing economies central banks began raising their key interest rates at the end of the year. The ECB's key interest rate has remained at 1.00% since May 2009, while the Fed's key interest rate has been in the interval between zero and 0.25% since December 2009. The two most important central banks are still implementing temporary non-standard measures. In November the Fed announced a second round of purchases of government securities in the amount of USD 600 billion, which is expected to be undertaken until the end of the second quarter of 2011. The ECB has also been making purchases of debt securities since May (see Box 1). The euro exchange rate against the US dollar was volatile in 2010, but overall the euro lost 4.8% to average USD 1.33. The euro fell in the first half of the year primarily as a result of expectations of faster growth in the US economy. It then rose until October, primarily as a result of favourable economic results in euro area in the second quarter and the anticipated announcement of a second round of quantitative easing by the Fed. The euro fell again in the final two months of 2010, as a result of further deterioration in the public finance situation in certain euro area periphery countries and their subsequent downgradings.

Figure 5: **Euro-US dollar exchange rate and key ECB and Federal Reserve interest rates**



Sources: ECB, Federal Reserve

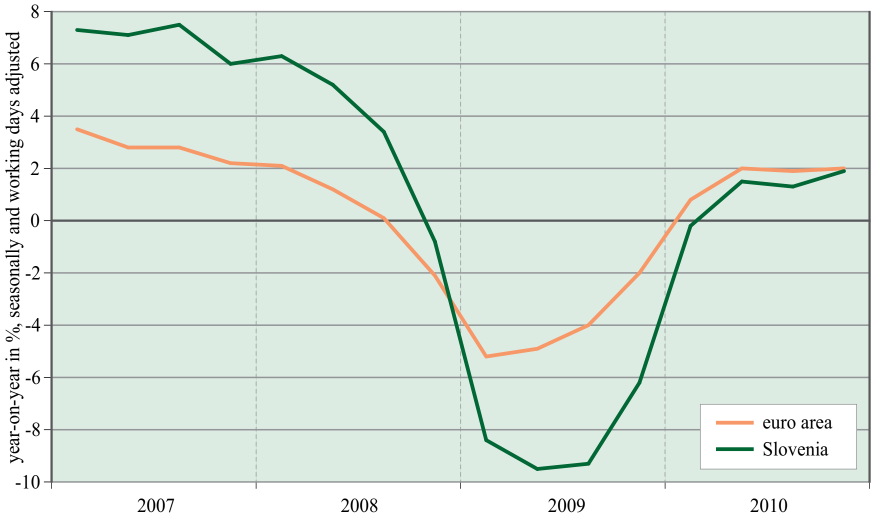
Slovenia's economic growth of 1.2% in 2010 was below the euro area average, primarily as a result of the deepening crisis in construction.

Slovenia's economic growth of 1.2% in 2010 was less than the euro area average, primarily as a result of the deepening crisis in construction and adverse developments in financial intermediation. With construction investment again falling, value-added in construction declined for the second consecutive year, by around 15%. The economic and financial crisis also began to be reflected, with a lag of one year, in value-added in financial intermediation, which declined by 3% last year. Growth in value-added was positive in the vast majority of other sectors, the highest growth being recorded by sectors mostly dependent on foreign demand. Growth reached 8% in manufacturing, and just under 6% in transportation, storage and communications. Growth in final household consumption turned positive, albeit barely, as the situation on the labour market deteriorated further in 2010. Consumer purchasing power as measured by the real gross wage bill declined for the second consecutive year. Growth in final government consumption declined to just under 1%, primarily as a result of public finance consolidation measures. With domestic consumption recording positive but low growth last year, the positive contribution to GDP growth made by net trade declined, the decisive contribution coming from the renewal of inventories. As a

Foreign demand was again the key growth factor in 2010.

result of the adverse situation on the labour market and public finance consolidation, the majority of economic growth in Slovenia will remain based on exports, as a result of which maintaining the right macroeconomic policies to ensure price and cost competitiveness is of key importance to Slovenia's economic performance.

Figure 6: **GDP growth in Slovenia and the euro area**

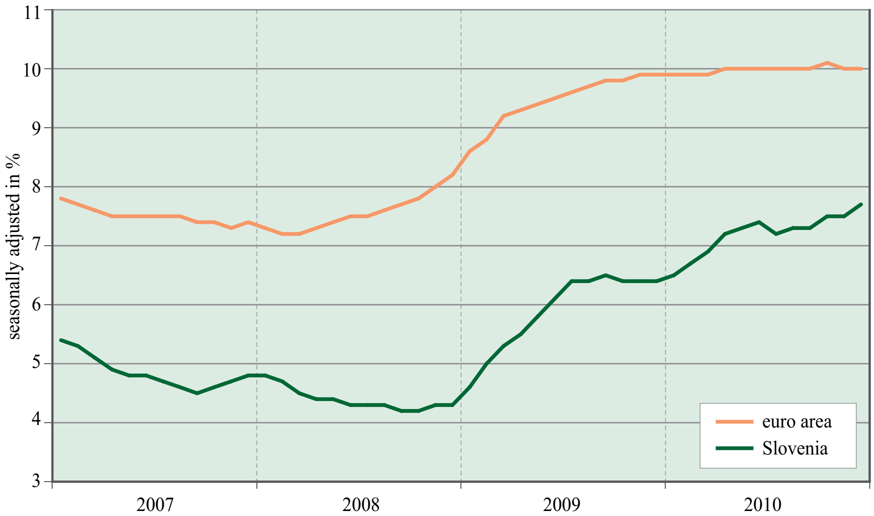


Source: Eurostat

2010 saw another large fall in employment.

Because the labour market responds to economic activity with a lag, employment continued to fall in 2010. After falling by 1.9% in 2009, total employment fell by a further 2.2% in 2010. The largest falls in employment were recorded by manufacturing and construction, at 6.3% and 9.5% respectively. The fall in employment in the total economy was mitigated by employment in the public sector, where the number of employees was up 1.8% in 2010, the education sector recording the largest rise. The number of registered unemployed was up around 16% or 14,000 overall in 2010, ending the year at more than 110,000. The harmonised unemployment rate in Slovenia rose sharply again in 2010, in contrast to the euro area overall, ending the year at 7.7%.

Figure 7: **Harmonised unemployment rate in Slovenia and the euro area**

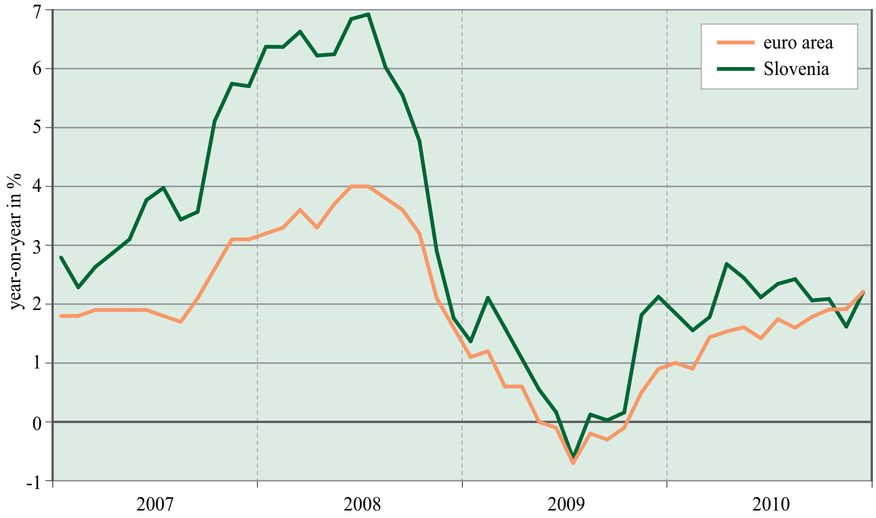


Source: Eurostat

Inflation in Slovenia stood at 2.1% in 2010, 0.5 percentage points higher than the euro area overall.

Average inflation as measured by the HICP stood at 2.1% in 2010, up 1.2 percentage points on 2009, and 0.5 percentage points more than the euro area average. The main factor in the rise was energy prices, particularly as a result of rises in oil prices on global markets, and rises in excise duties on electricity, natural gas and motor fuels. Meanwhile, the core inflation indicators remained low or even fell further in 2010, and were significantly below the euro area average. Growth in services prices slowed, while prices of manufactured goods actually fell on average.

Figure 8: **Inflation in Slovenia and the euro area**

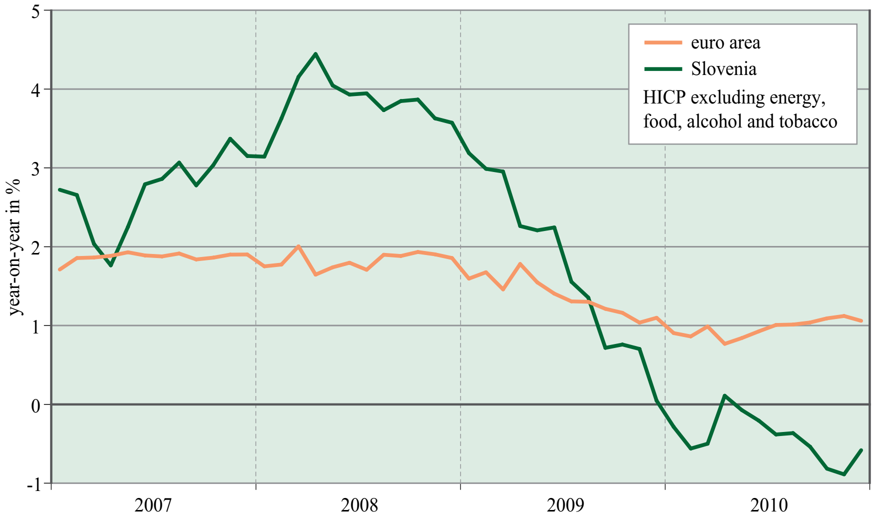


Sources: Eurostat, Bank of Slovenia calculations

Core inflation in 2010 was lower than in the euro area, partly as a result of an above-average fall in car prices and changes in the measurement of certain prices.

Core inflation as measured by the HICP excluding energy, food, alcohol and tobacco stood at -0.4% in 2010, down 2.1 percentage points on its 2009 average, and 1.4 percentage points less than the euro area average. The other two core inflation indicators, inflation excluding energy and inflation excluding energy and unprocessed food, were below the euro area averages in 2010, by approximately 0.7 percentage points. Core inflation in Slovenia and the euro area was influenced by the slow recovery in economic activity and the adverse situation on the labour market, which had a negative impact on final household consumption. There were several specific factors in core inflation being lower in Slovenia, including an above-average fall in car prices and a slowdown of growth in services prices, partly as a result of changes in the measurement of school meal prices.

Figure 9: **Core inflation in Slovenia and the euro area**



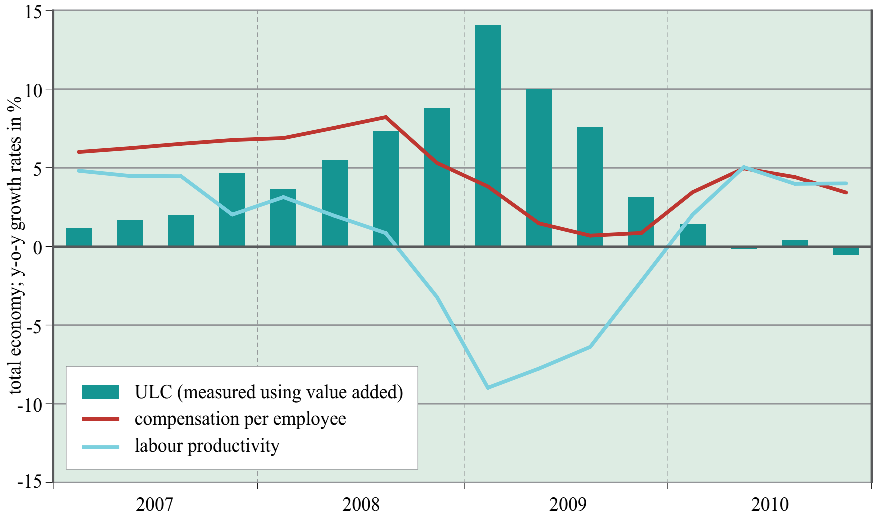
Sources: Eurostat, Bank of Slovenia calculations

Growth in unit labour costs declined sharply in 2010 …

Having increased sharply in the two previous years, growth in unit labour costs slowed significantly in 2010. The slowdown was primarily the result of a reversal in the trend in productivity, year-on-year growth in productivity having fallen sharply in 2009, before turning positive again in early 2010. The main factors in the rise in labour productivity were the increase in value-added and the continuing fall in employment. Growth in labour productivity was highest in the second quarter of 2010, when GDP increased by 2%, and output per employee was up 5.0% in year-on-year terms. Although year-on-year growth in labour costs per employee increased significantly in 2010, it remains moderate relative to the high productivity growth and the one-off effects of changes in employment structure. Year-on-year growth in the average gross wage increased from 1.8% in 2009 to 5.1% in the private sector overall, and from 0.9% in 2009 to 8.9% in manufacturing. The major factors in the increased growth were the statistical effect of the rise in the average wage in the private sector as a result of extensive lay-offs among the low-paid, a rise in the minimum wage, and a rise in wages for employees whose wages were temporarily reduced during their inclusion in the government measure to subsidise temporary lay-offs. By contrast, growth in labour costs in the public sector declined significantly: growth in the average gross wage stood at 6.6% in 2009, as a result of the introduction of the new wage system, but 0.0% in 2010.[4] In light of these developments, growth in unit labour costs in the total economy stood at just 1.4% in the first quarter of 2010, and stagnated in the other three quarters. A similar picture is presented by Slovenia's labour costs relative to the euro area. According to these figures, Slovenia's competitiveness deteriorated just slightly in 2010.

[4] According to this indicator, the public sector comprises the sectors of public administration, education, health and culture under the NACE Rev. 2.

Figure 10: **Labour productivity, unit labour costs and compensation per employee in the Slovenian economy**



Sources: Eurostat, Bank of Slovenia calculations

… but not enough to improve the cost competitiveness of the economy.

Growth in labour costs has a direct impact on the cost competitiveness of the economy, and also indirectly on its price competitiveness, via the effect on the level of prices. For long-term sustainability in the macroeconomic equilibria it is vital that the level of costs relative to productivity and the level of prices do not show a sustained deviation from the level that ensures corporate competitiveness on the market. Cost competitiveness and price competitiveness indicators show a deviation in the direction of appreciation, i.e. a deterioration in competitiveness, relative to the average of other euro area countries. After a sharp upward deviation in 2009, growth in unit labour costs slowed significantly in 2010, the year-on-year deterioration in competitiveness as measured by the real harmonised indicator diminishing. The average cost adjustment of the Slovenian economy to the crisis situation was nevertheless less than the euro area average. The main factors in this were the above-average fall in GDP and the slow adjustment of the labour market. Further delays in the cost adjustment of the economy could bring a further slowdown in economic growth via a decline in investment activity, sustained high unemployment and loss of market share in international trade.

Figure 11: **Harmonised competitiveness indicator adjusted for inflation using the HICP and ULC**

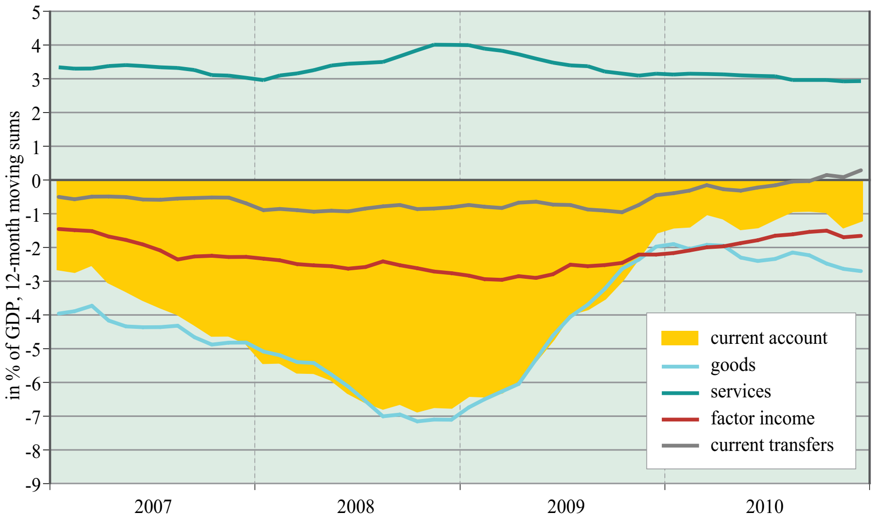
Source: ECB

The current account deficit declined to 1.5% of GDP in 2009, primarily as a result of low domestic consumption and a decline in net interest payments to the rest of the world. In 2010 the further narrowing of the current account deficit slowed, under the influence of a deterioration in the terms of trade. The deficit stood at 1.1% of GDP last year. The rapid growth in foreign demand brought notable increases in merchandise exports and imports of intermediate goods for the needs of industry in the first three quarters of the year. Domestic demand also increased slightly in the final quarter, and thus imports of goods for domestic final consumption. Merchandise exports were up 10.2% overall in 2010 in volume terms, 2.5 percentage points more than the rise in merchandise imports. However, as a result of price factors, the merchandise trade deficit widened by 0.7 percentage points to 2.7% of GDP. The faster growth in import prices began in the second quarter of 2010, and peaked in the final quarter as a result of rapid growth in commodity prices on global markets. Import prices rose by 6.4% in 2010, and export prices by 3.0%, the terms of trade thereby deteriorating by 3.2% relative to 2009. This contributed 1.7% of GDP towards the trade deficit. Growth in trade in services, tourism in particular, was strongly outpaced by growth in merchandise trade. With imports growing faster, the surplus of trade in services narrowed from 3.1% of GDP to 2.9% of GDP in 2010. Current transfers were also a major factor in the smaller current account deficit, with net outflows of factor income down a fifth in association with lower expenditure on interest payments on loans raised in the rest of the world. Faster disbursement of EU funds at the end of last year meant that current transfers swung from a deficit of 0.4% of GDP in 2009 to a surplus of 0.3% of GDP in 2010.

The current account deficit stood at 1.1% of GDP in 2010, primarily as a result of a deterioration of 3.2% in the terms of trade.

The main factors in the narrowing of the deficit compared with 2009 were the decline of a fifth in net outflows of factor income and the faster disbursement of EU funds.

Figure 12: **Components of the current account**



Source: Bank of Slovenia

After a longer period of declining indebtedness, the private sector[5] again recorded net financing in the rest of the world in 2010. The net inflows amounted to EUR 310 million, primarily as a result of an increase in FDI and portfolio investments. On the claim side, the largest decline was in the banks' claims on the basis of currency and deposits. Loans made by domestic banks to the rest of the world also declined, by EUR 143 million. The rapid growth in merchandise trade has begun to drive up financing via trade credits. Households and corporates increased their portfolio investments in equities and debt securities in the rest of the world, while the banks reduced them as a result of the adverse situation on the banking market.

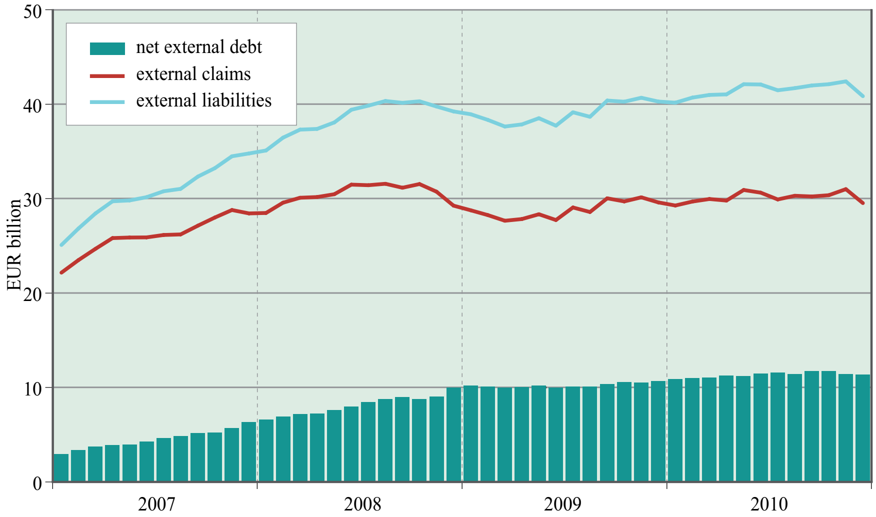
In 2010 the private sector again recorded net financing in the rest of the world, primarily as a result of an increase in FDI and portfolio investments.

5 The private sector is defined as the total economy excluding the Bank of Slovenia and the general government sector.

The banking sector and the government sector increased their net external debts, while other sectors, including the Bank of Slovenia, recorded a decline in net external debt.

There was also a sharp increase in FDI on the liability side as a result of certain corporate sales. The largest increase in the non-residents' investments in private sector securities was the result of SID banka's bond issue of EUR 750 million. The decline in the domestic banks' indebtedness to banks in the rest of the world and to the ECB, and to a lesser extent the decline in corporate indebtedness to the rest of the world continued in 2010. The gross external debt increased by EUR 0.7 billion in 2010 to reach EUR 40.9 billion at the end of the year, while gross external claims were up EUR 0.25 billion at EUR 29.5 billion. This resulted in the net external debt increasing by EUR 0.4 billion to EUR 11.3 billion. The main contributions to the increase in the net external debt came from the banking sector and the government sector, while the Bank of Slovenia and other sectors reduced their net debt to the rest of the world.

Figure 13: **Slovenia's external debt**

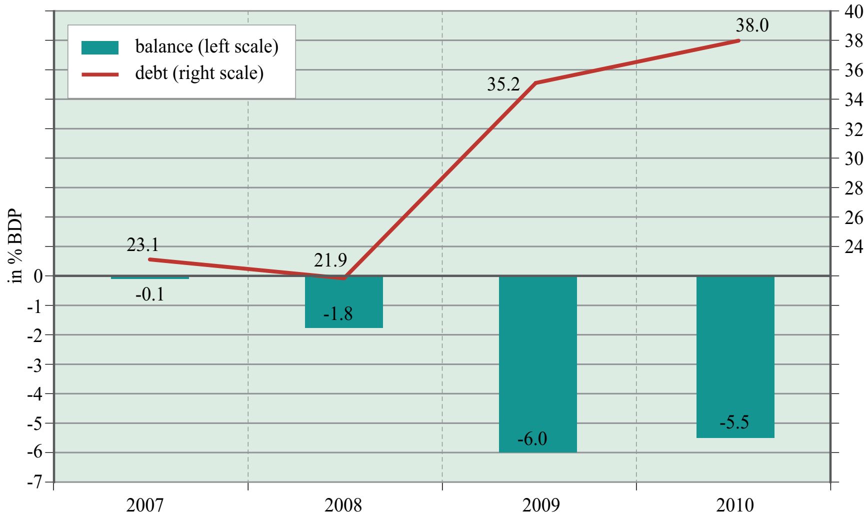


Source: Bank of Slovenia

As a result of the continuing large general government deficit in 2010, the general government debt increased, but remained significantly below the euro area average.

The general government deficit according to the ESA 95 stood at 5.5% of GDP in 2010, down 0.5 GDP percentage points on the previous year. The persistence of a large general government deficit in 2010 was the result of low economic growth and further deterioration in the situation on the labour market. After recording a year-on-year decline in the first quarter, general government revenues increased over the rest of the year, taking the increase over the whole of the year to 2.8%. Direct taxes were down slightly on 2009, partly as a result of a cut in the corporate income tax rate and an increase in the general allowance for personal income tax. During the year the government raised excise duties on all types of products subject to duty, as a result of which excise duty revenues in 2010 were slightly higher than in the previous year. General government expenditure increased by 1.8% in 2010, less than the increase in general government revenues. The increase was significantly less than in previous years, primarily as a result of measures taken within the framework of the Economic Crisis Intervention Measures Act, which restricted growth in expenditure on wages, pensions and social transfers. Last year also saw low growth in expenditure on intermediate consumption, while expenditure on investment declined, while expenditure on interest and expenditure on the unemployed continued to increase sharply. The general government debt stood at EUR 13,704 million at the end of 2010, or 38.0% of GDP. The debt was up again, despite the use of pre-financing funds, while borrowing was primarily undertaken in the first quarter of 2010 via the issue of long-term bonds with a nominal value of EUR 2.5 billion.

Figure 14: **General government deficit and debt according to ESA95 methodology**

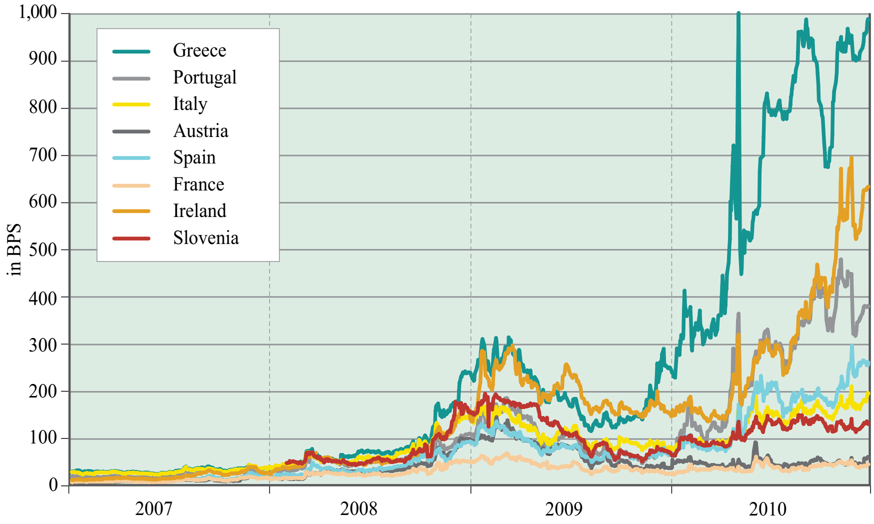


Source: SORS

Consistent implementation of fiscal consolidation is vital to the retention of a favourable position in sovereign debt markets.

In 2010 Slovenia joined the programme of financial assistance to Greece, and the programme to ensure financial stability in the euro area. The yield spreads of the 10-year government bonds of certain euro area countries over the benchmark German bond increased sharply in 2010, particularly in countries with a poor public finance position. A mechanism of financial assistance to Greece was agreed in May 2010, and then at the end of the year Ireland asked for assistance from the European Financial Stability Facility (EFSF). Slovenia approved a loan of EUR 102.8 million for Greece in September, while its total lending over a period of three years is limited to EUR 388 million. In July 2010 the National Assembly adopted the Act on Guarantees of the Republic of Slovenia for the Purpose of Maintaining Financial Stability in the Euro Area, which ensured Slovenia's participation in the EFSF. Slovenia's total guarantee commitments within the framework of the EFSF could amount to a maximum of EUR 2,073 million. The spreads of Slovenian 10-year government bonds over the German benchmark bonds showed no significant change after summer 2010, and stood at around 120 basis points. At the end of the year Standard & Poor's left its ratings for Slovenia unchanged at AA for long-term debt and A-1+ for short-term debt, but downgraded the outlook from stable to negative. The negative outlook entails the possibility of a downgrading in the next two years, which could occur if the government fails to stabilise the government debt. Successful and timely fiscal consolidation is thus vital to maintaining a favourable position on sovereign debt markets.

Figure 15: **Spreads of 10-year government bonds over benchmark German bonds**



Sources: Bloomberg, Bank of Slovenia calculations

Notes: Spreads are calculated as the difference between yields on 10-year government bonds and the yield on the benchmark (German) bond on a daily basis, and reflect the additional risks that the markets ascribe to countries as debtors. The movement of the SLOREP 01/20 bond is shown for Slovenia after 18 January 2010.

Given the large general government deficit and the rise in the general government debt, which are nevertheless behind the euro area average, Slovenia remained in the excessive deficit procedure[6] last year, as it has since December 2009. Slovenia must reduce the excessive deficit to below 3% of GDP by 2013. Fiscal consolidation is therefore vital for Slovenia, and is a government priority. The effective implementation of structural reforms will also be important in the achievement of long-term sustainable economic growth.

Banking system

There was no significant change in the ownership structure of the banking system in 2010.

At the end of 2010 there were 19 banks operating in Slovenia, of which eight were subsidiaries, three branches of foreign banks, and three savings banks. Banks accounted for 99.1% of the sector in terms of total assets. There was no change in the number of credit institutions from the previous year. At the end of 2010 there were eight subsidiary banks and three branches of foreign banks that were under majority foreign ownership, one bank under full domestic ownership, and nine banks under majority domestic ownership. The proportion of total bank equity held by non-residents was up 0.5 percentage points in 2010 at 37.1%. Counting only non-residents that hold more than 50% of the equity in an individual bank, the figure is 27.8%. Government ownership as measured by equity declined slightly last year, to stand at just over 20% at the end of the year.

The banking system's total assets declined by EUR 1.3 billion in 2010 to EUR 50.3 billion.

The banking system's total assets declined by EUR 1.3 billion last year to EUR 50.3 billion or 140% of GDP. Total assets finished the year down 2.5%. The main reasons for the decline in total assets were the banks' continuing debt repayments to banks in the rest of the world, the repayment of funding obtained in Eurosystem

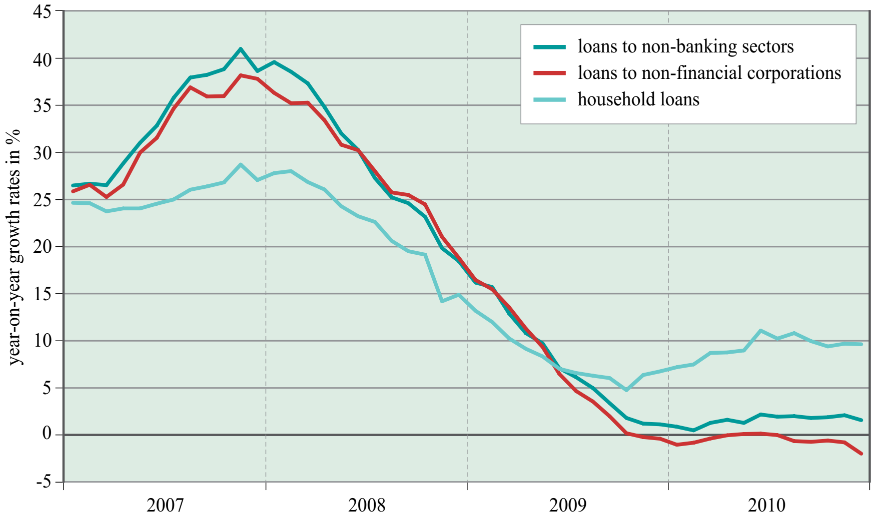
6 The excessive deficit report, which is the first step in the excessive deficit procedure, was adopted for Slovenia by the European Commission in October 2009 on the basis of the finding that its general government deficit during that year had exceeded the reference value of 3% of GDP. In December 2009 ECOFIN then adopted a Council Decision on the existence of an excessive deficit in Slovenia, and Council Recommendations to rectify the excessive deficit. In July 2010 the European Council assessed Slovenia, like the other EU Member States in the excessive deficit procedure, as taking appropriate action to rectify the excessive deficit.

LTROs, and the withdrawal of government deposits. The banks were unable to fully replace this funding by means of securities issues. Last year's increase in household deposits at banks was significantly lower than those in the pre-crisis years.

The banks adjusted to the decline in debt on the liability side of the balance sheet by reducing their investments in securities and investments at banks, and by curbing growth in loans to non-banking sectors. The banks' loans to non-banking sectors increased by just EUR 536 million in 2010. This primarily comprised loans to households, while the stock of corporate loans actually declined.

The banks adapted to the decline in debt on the liability side by reducing investments in securities and investments at banks, and via a stagnation in corporate lending.

Figure 16: **Lending to non-banking sectors**



Source: Bank of Slovenia

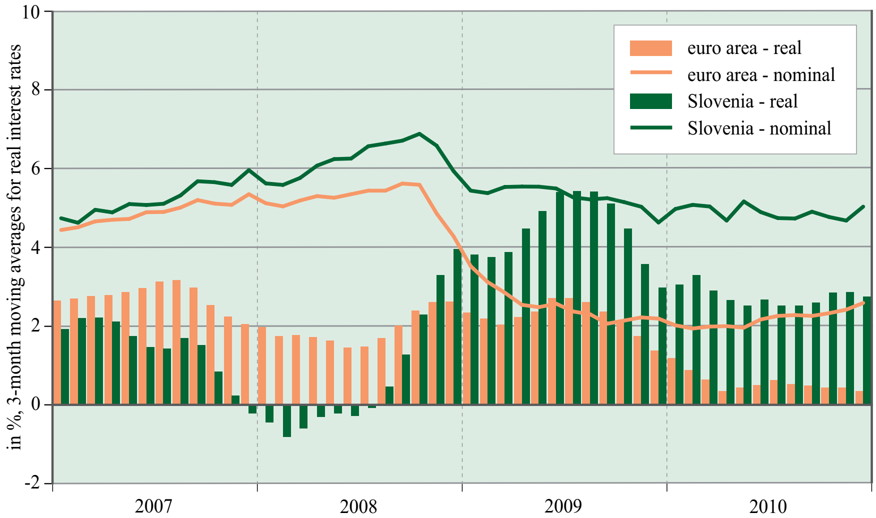
There were notable differences in growth in loans to different sectors in 2010. Year-on-year growth in loans to non-banking sectors averaged below 2%. The average was negative for corporate loans (-0.6%), the rate ending the year at -2%. The average for household loans was relatively high, at more than 9%. The main factors in the decline in corporate loans were high corporate indebtedness and the related low creditworthiness, the rising cost of loan collateral and the maintenance of high premiums over reference interest rates. An additional factor in the decline in the stock of corporate loans was the banks' creation of large impairments. All the bank groups saw a decline in growth in loans, although the domestic banks maintained positive growth, while the banks under majority foreign ownership recorded negative growth. While reducing their corporate loans, the banks under majority foreign ownership also recorded an above-average increase in household loans in 2010. The banks primarily approved short-term loans to corporates, while for households it was long-term loans that prevailed, housing loans in particular. Year-on-year growth in housing loans stood at 23% at the end of 2010. The stock of consumer loans declined last year.

The low growth in loans that was a feature of 2010 was partly the result of low corporate creditworthiness.

Banks in Slovenia maintained high nominal interest rates on corporate loans in 2010. Nominal interest rates on corporate loans in Slovenia were significantly higher than in the euro area overall. The spread on loans of more than EUR 1 million stood at around 2.7 percentage points last year. The main reasons for interest rates remaining high in Slovenia were the continuing adverse situation in funding in the rest of the world, the banks' tendency to respond to increased impairment and provisioning costs by raising interest rates, and the relatively high indebtedness of Slovenian corporates, which led to increased credit risk. With average inflation rising, real interest rates on corporate loans declined in 2010, although this had no impact on lending.

Interest rates on corporate loans in Slovenia were higher than those in the euro area overall, and the spread did not diminish in 2010.

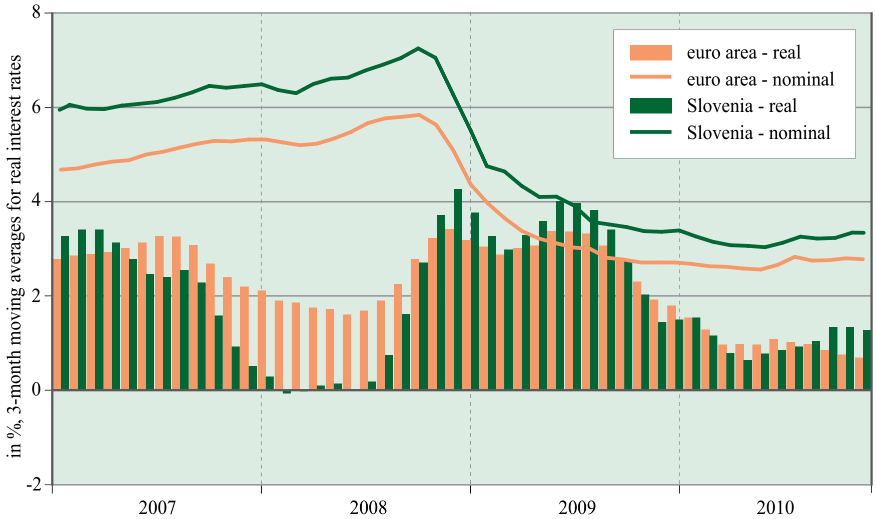
Figure 17: **Interest rates on loans of more than EUR 1 million for non-financial corporations**



Sources: ECB, Bank of Slovenia

Interest rates on consumer loans were lower in nominal terms and real terms than the comparable interest rates in the euro area overall. Interest rates on housing loans were 0.5 percentage points higher on average than the comparable interest rates in the euro area overall in nominal terms, a smaller spread than in 2009. Real interest rates on housing loans were lower than the euro area average until the end of the summer, but overtook them in September and remained higher.

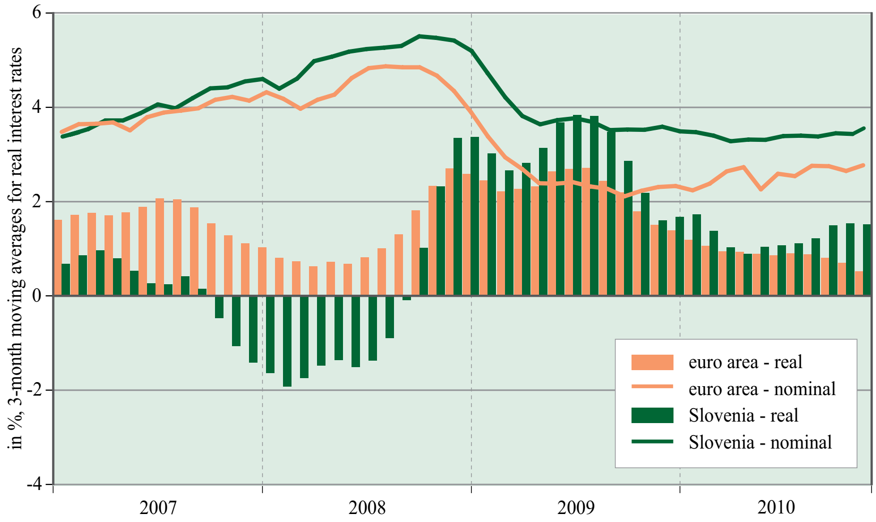
Figure 18: **Interest rates on housing loans to households**



Sources: ECB, Bank of Slovenia

Nominal interest rates on deposits of up to 1 year, which account for the majority of household deposits, were lower in Slovenia last year than the comparable rates in the euro area overall, having been higher the previous year. Interest rates on household deposits of more than 1 year at banks in Slovenia last year remained higher than at euro area banks overall. The spread on deposits of 1 to 2 years, where the increase in household deposits was largest, averaged 0.9 percentage points, down on the previous year. With the banks' funding in the rest of the world declining and the banks making repayments of liabilities to banks in the rest of the world and to the Eurosystem, deposits by non-banking sectors are the most important source of funding, particularly at the banks under majority domestic ownership.

Figure 19: **Interest rates on household deposits of 1 to 2 years**



Sources: ECB, Bank of Slovenia

The deterioration in the economic situation in 2010 had a significant adverse impact on the banks' performance. According to provisional unaudited figures, the banking system's pre-tax loss amounted to EUR 96.4 million in 2010. The banks were unable to reduce these losses by raising net interest income or cutting operating costs. Net interest income last year was up 11.3% on the previous year, while non-interest income was down 11.2%. The main factor in the decline in non-interest income was losses on financial assets held for trading, on which the banks recorded gains in the previous year. As a result of all this, the banks' gross income only increased slightly last year.

According to unaudited figures, the banking system operated at a loss in 2010, recording a loss of EUR 96 million.

Table 1: **The banking system's income statement**

	Amount (EUR million)				Growth rate, %				Proportion of gross income, %			
	2007	2008	2009	2010	2007	2008	2009	2010	2007	2008	2009	2010
Net interest	816.4	944.6	932.2	1037.7	18.3	15.7	-1.3	11.3	57.0	69.4	65.4	70.3
Net non-interest income	616.7	415.6	493.1	437.9	17.3	-32.6	18.7	-11.2	43.0	30.6	34.6	29.7
Gross income	1,433.0	1,360.2	1,425.3	1,475.6	17.9	-5.1	4.8	3.5	100.0	100.0	100.0	100.0
Operating costs	755.9	776.0	765.2	765.9	7.7	2.7	-1.4	0.1	52.7	57.1	53.7	51.9
Labour costs	401.8	412.1	415.5	413.3	9.4	2.6	0.8	-0.5	28.0	30.3	29.1	28.0
Net income	677.1	584.2	660.2	709.7	31.9	-13.7	13.0	7.5	47.3	42.9	46.3	48.1
Net provisioning and impairments	163.0	277.9	499.6	806.1	36.0	70.5	79.8	61.3	11.4	20.4	35.1	54.6
Pre-tax profit	514.2	306.3	160.5	-96.4	30.6	-40.4	-47.6	...	35.9	22.5	11.3	...
Taxes	102.5	58.6	38.7	-2.1	12.8	-42.8	-33.9	...	7.1	4.3	2.7	...
Net profit	411.7	247.7	121.8	-94.3	36.0	-39.8	-50.8	...	28.7	18.2	8.5	...

Source: Bank of Slovenia

The banks' operating costs remained unchanged last year, while labour costs declined slightly. In 2010 the banks created EUR 806 million of impairments and provisions, up 61% on the previous year. The ratio of impairment and provisioning costs to gross income increased by almost 20 percentage points to 54.6%, compared with a pre-crisis level of just 11.4%.

Table 2: **Bank performance indicators**

In %	2006	2007	2008	2009	2010
ROA	1.25	1.36	0.67	0.32	-0.19
ROE	15.10	16.30	8.10	3.90	-2.30
Operating costs on average total assets	1.54	1.54	1.54	1.54	1.54
Interest margin on interest-bearing assets	2.35	2.32	2.20	1.99	2.13
Interest margin on total assets	2.18	2.15	2.08	1.88	2.02
Non-interest margin	1.67	1.63	0.92	0.99	0.85
Gross income on average assets	3.85	3.78	3.00	2.87	2.87

Source: Bank of Slovenia

The increase in credit risk at banks was expressed in a deterioration in the quality of the banking system's investments.

The increase in credit risk continued last year, and was expressed in a significant deterioration in the quality of the banks' investments. Clients' arrears in settling their liabilities to banks increased significantly, particularly in certain sectors. The largest proportions of classified claims more than 90 days in arrears at the end of 2010 were recorded by the sectors of information and communication activities, and construction, where the figure was just over 19%. The overall proportion of classified claims more than 90 days in arrears increased from 6.6% to 12.3%. At the same time the deterioration in the quality of investments was expressed in downgradings from the highest ratings of A and B to lower ratings, an increase in the proportion of non-performing claims and an increase in the coverage of claims by impairments.

There was no significant change in the banking system's capital adequacy last year. The capital adequacy ratio stood at 11.3% at the end of the year.

As a result of the pronounced increase in impairment and provisioning costs, the stagnation in lending and the decline in non-interest income, the banks' significantly increased income risk was seen in the banking system's losses. Interest rate risk increased slightly, but remained below its pre-crisis level. There was no significant change in the banking system's liquidity risk. The banks maintained relatively high first-bucket liquidity ratios, but there was a slight decline in the second-bucket liquidity ratio. Secondary liquidity declined by EUR 0.8 billion, primarily as a result of adjustments on the investment side of the balance sheet to changes on the funding side, although at the same time the decline entailed secondary liquidity approaching the level typical of the pre-crisis period. The banks remain exposed to refinancing risk, which could increase if the financing conditions were to deteriorate. Slovenia's banking system has so far maintained an adequate level of solvency, despite the adverse situation. The overall capital adequacy ratio stood at 11.3% at the end of 2010, while the Tier 1 capital adequacy ratio stood at 9.0%.

Table 3: **Ratings breakdown of classified claims and coverage of claims by impairments and provisions**

	31. Dec 2008			31. Dec 2009			31. Dec 2010		
	Classified assets	Impair-ments	Coverage of claims by impair-ments (%)	Classified assets	Impair-ments	Coverage of claims by impair-ments (%)	Classified assets	Impair-ments	Coverage of claims by impair-ments (%)
Total in EUR million	47,129	1,403	3.0	49,757	1,827	3.7	50,290	2,420	4.8
	Structure (%)			Structure (%)			Structure (%)		
A	74.4	8.8	0.4	70.7	7.0	0.4	70.9	5.7	0.4
B	22.7	34.4	4.5	24.5	30.8	4.6	21.2	19.9	4.5
C	1.0	8.7	24.8	2.6	16.2	23.2	4.3	22.5	25.2
D	1.0	20.8	62.3	1.4	24.7	62.9	2.8	35.4	59.9
E	0.8	27.2	100.0	0.8	21.2	100.0	0.8	16.5	100.0

Source: Bank of Slovenia

2 BANK OF SLOVENIA ACTIVITIES

2.1 Tasks in the scope of the ESCB

2.1.1 Institutional framework

The European Central Bank, the Eurosystem and the European System of Central Banks

With the introduction of the euro in Slovenia on 1 January 2007, the Bank of Slovenia became a part of the Eurosystem, which comprises the European Central Bank (ECB) and the national central banks of the euro area countries. Since the introduction of the euro in Slovenia, the Governor of the Bank of Slovenia has been a member of the Governing Council of the ECB, attending its meetings, which normally take place twice a month. The Governing Council comprises the six members of the Executive Board and the governors of the national central banks of the euro area countries. The responsibilities of the Governing Council include defining the monetary policy for the euro area. In addition, the Governor of the Bank of Slovenia is still a member of the General Council of the ECB, the third decision-making body of the ECB, which meets four times a year. The General Council comprises the President and the Vice-President of the ECB and the governors of the national central banks of all EU Member States.

Bank of Slovenia experts attended sessions of committees and their working groups in 2010, when meetings were conducted in the wider composition of the European System of Central Banks (ESCB), which comprises the ECB and the national central banks of all EU Member States, and in the narrower composition of the Eurosystem. The committees support the work of ECB decision-making bodies, which may request expert and technical advice from the committees.

The national central banks are the sole subscribers to and holders of ECB capital. Pursuant to the Statute of the ESCB and of the ECB, the shares of the national central banks in the ECB's capital key are weighted according to the proportion of the respective Member States in the total population and gross domestic product of the EU. The national central banks of the Member States that have introduced the euro have paid up their entire share of the ECB's capital. The other national central banks of EU Member States that have not yet introduced the euro have not paid up their entire share, but only a certain percentage of the amount that they would have to pay up had they introduced the euro. Since 29 December 2010 the contributions by national central banks of EU Member States that have not yet introduced the euro have constituted 3.75% of the subscribed capital. The ECB resolved on 29 December 2010 to increase its subscribed capital by EUR 5 billion, from EUR 5.76 billion to EUR 10.76 billion. It was resolved that the national central banks of the euro area would pay up their additional contribution to the ECB's capital in three annual instalments.

The Bank of Slovenia's key for subscription of the ECB's capital has been 0.3288% since 1 January 2009. The total amount of ECB capital paid up by the national central banks as at 29 December 2010 was EUR 5,305 million.

The Bank of Slovenia's key for subscription of the ECB's capital is 0.3288%.

2.1.2 Implementation of the Eurosystem's monetary policy

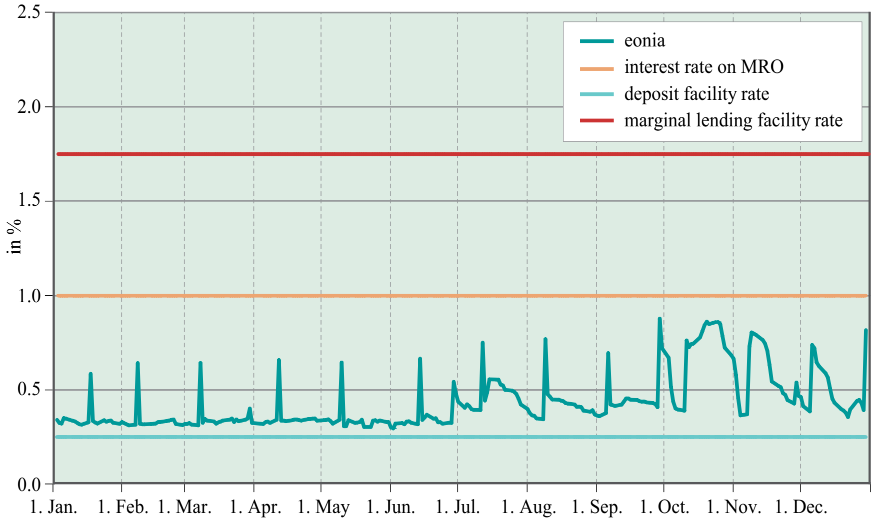
Additional non-standard monetary policy instruments.

In 2010 the euro area money market also felt the consequences of the financial turmoil that began in mid-2007.The situation worsened in May 2010 with the Greek sovereign debt crisis, and then further with Ireland in the autumn. The Eurosystem responded to the restrictions in access to funding on the financial markets, which were affecting an increasing number of banks because of the sovereign debt problems, by granting free access to Eurosystem loans for banks: since October 2008 the sole condition for a loan from the Eurosystem has been a sufficient quantity of eligible collateral.

Excess liquidity and increased volatility of the Eonia.

As a result of the sharp increase in banks' liquidity needs caused by the change in the situation on the money market, in October 2008 the Eurosystem introduced full allotment in open market lending operations. It is for this reason that the banks were faced with large excess reserves. In 2010 the Eonia was still below the key interest rate (1%), and was mostly close to the interest rate on the deposit facility (0.25 %, see Figure 20). Greater uncertainty surrounding the future liquidity situation as 1-year loans made in 2009 matured led to a greater volatility of the Eonia, and a higher average level than in 2009, although the key interest rate remained unchanged.

Figure 20: **ECB interest rates and Eonia**



Source: ECB

A detailed description of changes in the use of monetary policy instruments and the quantification of their relative importance in 2010, and an explanation of the use of collateral in monetary policy lending are given below.

Eurosystem monetary policy instruments in 2010

The three basic categories of monetary policy instruments are open market operations, standing facilities and minimum reserves. In normal circumstances, the Eurosystem uses minimum reserves to stabilise demand for liquidity, open market operations - reverse main refinancing operations (MROs), longer- term refinancing operations (LTROs) and fine-tuning operations (FTOs) - to provide the required amount of liquidity, and the deposit facility and marginal lending facility to smooth out any imbalances between supply of and demand for liquidity, thereby stabilising the Eonia in the corridor around the key interest rate.[7]

The highlights in 2010: continued full allotment, maturing of the 1-year LTROs, increased securities purchases.

Given the extraordinary situation, the open market operations and standing facilities in 2010 were very different from those in normal circumstances. As a result of full allotment in all operations (with one exception, see below), the average amount and average maturity of loans via open market operations depended on demand from banks, and were not set by the Eurosystem as they would normally be. In July, September and December 2010 banks repaid EUR 614.4 billion that they had borrowed in 2009 in three operations with a maturity of one year. The effect of purchases of securities in the amount of EUR 72.5 billion was neutralised through weekly tenders of fixed-term deposits. The deposit facility, which otherwise would be used by banks only exceptionally, was used daily because of excess liquidity.

Open market operations: MROs, LTROs and FTOs

Main refinancing operations (MROs) are loans of one week offered in weekly tenders. They are executed according to a preannounced tender calendar. In 2010 the Eurosystem held 52 tenders, all with full allotment at fixed interest rates known in advance. The average amount of an MRO was EUR 133.8 billion, compared with EUR 149.8 billion in 2009. Slovenian banks and savings banks participated in all the tenders. The average amount of an MRO for Slovenian banks and savings banks was EUR 5.4 million.

In normal circumstances, *longer-term refinancing operations (LTROs)* are aimed at providing banks with additional stable refinancing. These 3-month loans are offered in monthly tenders.

Contraction in frequency and maturity, but not in the proportion of LTROs.

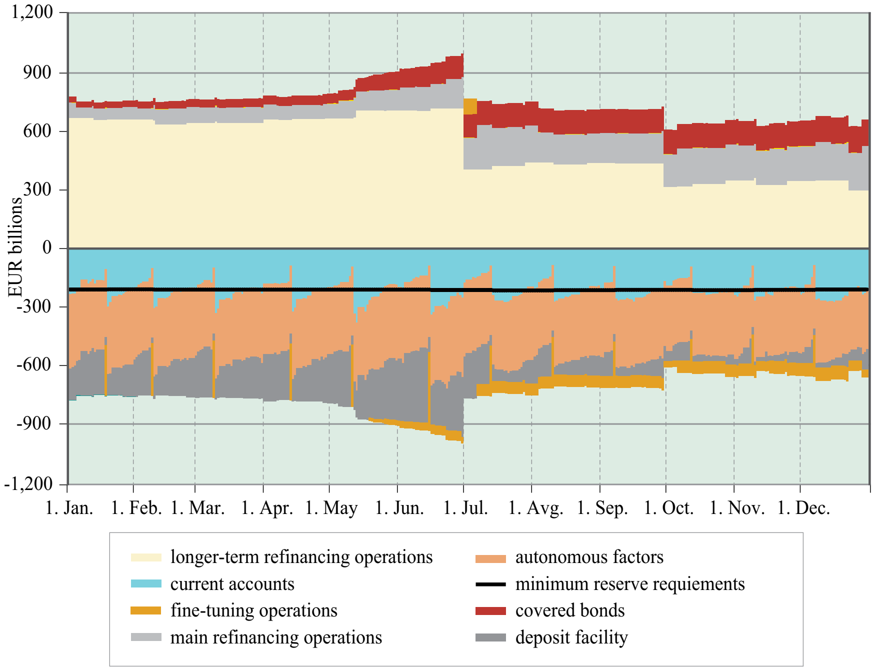
Between 2007 and 2009 the frequency of LTROs increased, while the range of maturities was expanded to 1-month, 6-month and 1-year operations. The Eurosystem gradually discontinued the supplementary LTROs during 2010. Two more with a maturity of six months were executed. The first, which had been announced at the end of 2009, was executed in late March, and the second in mid-May, as one of the responses to the deepening debt crisis in Greece. The interest rate in these operations was tied to the average key interest rate over the period to maturity, similar to the final 1-year LTRO in December 2009. In addition, in 2010 the Eurosystem executed in each month another tender for loans with a maturity equal to the minimum reserve maintenance period, i.e. between three and five weeks.

There were two other changes in relation to the LTROs. First, on the basis of the normalisation of the situation on the money market, the Eurosystem tried to phase-out full allotment for 3-month LTROs in April. April's LTRO was the first (and in 2010, the only) open-market lending operation since October 2008 where banks bid the amount and also the interest rate of the loan. Because the situation in the money market deteriorated drastically shortly afterwards as a result of the problems in Greece, the Eurosystem returned to full allotment in May. Second, with the aim of separating the implementation of monetary policy from the signalisation of the monetary policy stance, the LTROs in October, November and December were executed with an interest rate tied to the average key interest rate during the period to maturity of these LTROs.

7 The General Documentation on Eurosystem Monetary Policy Instruments and Procedures contains a detailed description of monetary policy instruments. This text is available on the ECB's website at http://www.ecb.int/pub/pdf/other/gendoc2008en.pdf.

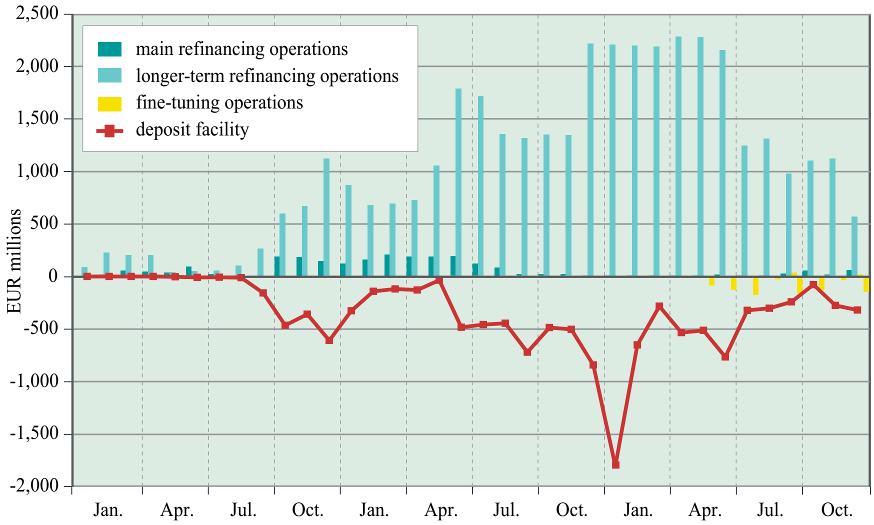
The outstanding amount of the LTROs averaged EUR 525.0 billion in 2010 (compared with EUR 554.8 billion in 2009), partly as a result of heavy participation by banks in the three 1-year operations a year earlier (see Figure 21). Measured as a proportion of the liquidity deficit of the Eurosystem, LTROs remained the main source of liquidity provision in 2010. A total of EUR 2,611 million in LTROs matured for Slovenian banks and savings banks in 2010, and a total of EUR 1,037 million was renewed in 12 such operations (see Figure 22). The maturity breakdown of the operations meant that the average outstanding amount of LTROs in 2010 was EUR 1,596 million, up by EUR 450 million from the 2009 average. The outstanding amount of LTROs was EUR 539 million at the end of 2010, compared with EUR 2,114 million on the final day of 2009.

Figure 21: **Supply of (+) and demand for (–) Eurosystem liquidity**



Source: ECB

Figure 22: **Outstanding amounts of Eurosystem monetary policy instruments, 2008 to 2010: Slovenian banks and savings banks (at month-end)**



Source: Bank of Slovenia

Fine tuning operations (FTOs) are executed by the Eurosystem on an ad hoc basis with the aim of countering liquidity imbalances in the market and thus stabilising interest rates. In 2010 these operations were used in three forms. First, they were used as tenders of fixed-term overnight deposits on the last day of the reserve maintenance period to equalise the banking system's actual liquidity with the required liquidity (determined by the banks' minimum reserves and any desired excess reserves). The average amount accepted in the 12 operations was EUR 231.8 billion. Slovenian banks and savings banks, which deposited of EUR 337 million on average, regularly participated in these tenders.

FTOs carried out on the final day of the reserve maintenance period, to diversify the maturity of LTROs and to sterilise securities purchases.

Second, upon the maturity of large LTROs, 1-year LTROs in particular, the Eurosystem offered banks on four occasions to borrow liquidity with the aim of diversifying the refinancing of maturing liquidity across several operations. These loans had maturities of six to 13 days, and always matured on the day of settlement of a main refinancing operation. All operations were executed with full allotment and at the key interest rate. The average amount allotted in these tenders was EUR 43.5 billion, with Slovenian banks and savings banks recording an average of EUR 11.3 million.

Third, to compensate for the increase in liquidity caused by purchases of securities, the Eurosystem took 1-week fixed-term deposits from banks at tenders carried out once a week starting in May. The offered amount was the same as the cumulative amount of securities purchased by the time in question, i.e. from EUR 16.5 billion in May to EUR 72.5 billion at the end of the year. With the exception of two tenders, banks submitted more bids than the amount offered by the Eurosystem. Slovenian banks and savings banks also participated in these tenders.

Other open market operations: CBPP, SMP, lending in foreign currencies

In accordance with a decision in May 2009 on the introduction of the *Covered Bond Purchase Programme (CBPP [8])*, the Eurosystem purchased covered bonds in 2010. Its purchases of EUR 60 billion of covered bonds by the end of June 2010 helped to revive the primary market, to increase the liquidity of the bonds, and to trigger the first issue of covered bonds in certain countries.

The Covered Bonds Purchase Programme was successfully completed at the end of June.

The key measure by which the Eurosystem tackled the consequences of the worsening sovereign debt crisis in 2010 was the Securities Markets Programme (SMP[9]). The programme is described in Box 1.

Box 1: **Securities markets programme**

In view of the severe tensions in certain market segments, on 10 May 2010 the Eurosystem announced interventions in the form of purchases in the euro area public and private debt securities markets. The Governing Council of the ECB took this decision in light of the declaration by EMU governments that they would take all measures needed to meet the fiscal targets in 2010 and in the years ahead, in line with excessive deficit procedures. The governments of certain EMU countries additionally committed themselves to accelerating fiscal consolidation and ensuring the sustainability of public finances.

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8 The Decision of the ECB on the implementation of the covered bond purchase programme (ECB/2009/16) represents the legal basis for this. The text is available on the ECB's website at http://www.ecb.int/ecb/legal/pdf/en_decision_ecb_2009_16.pdf.

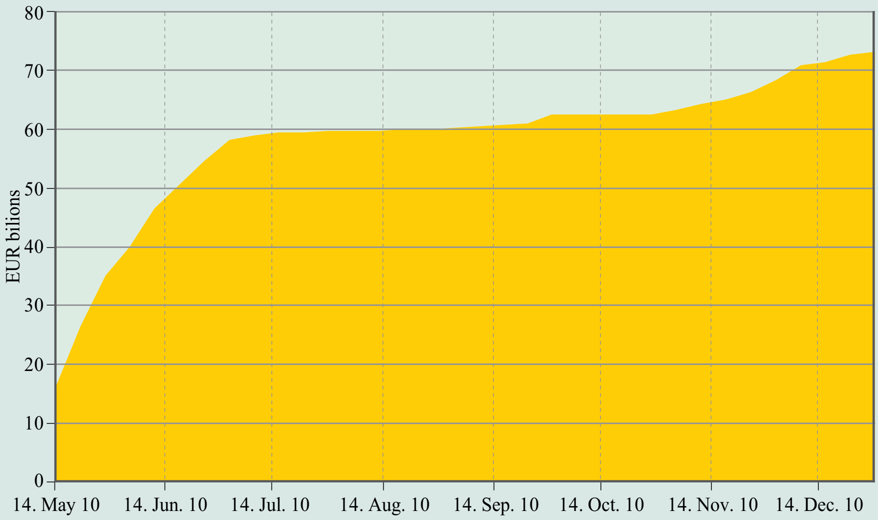
9 The Decision of the ECB establishing a securities markets programme (ECB/2010/5) represents the legal basis for this. See http://www.ecb.int/ecb/legal/pdf/l_12420100520en00080009.pdf

The SMP is a temporary monetary policy instrument. The Governing Council of the ECB decides on the scope of the interventions. The main objectives of the interventions are (1) to improve the functioning of certain segments of the bond market, and (2) to restore an appropriate monetary policy transmission mechanism and the effective conduct of monetary policy oriented towards price stability in the medium term. Interventions are executed by central banks of the Eurosystem in coordinated way. The impact of the interventions on liquidity is sterilised by the use of weekly liquidity absorbing FTOs. This ensures that the interventions do not affect the level of liquidity in the banking system and the money market interest rates.

In accordance with the Decision of the ECB establishing a securities markets programme (ECB/2010/5), Eurosystem central banks may purchase the following: (a) on the secondary market, eligible euro-denominated marketable debt instruments issued by the central governments or public entities of the EMU countries, and (b) on the primary and secondary markets, eligible euro-denominated marketable debt instruments issued by private entities incorporated in the euro area. This is in accordance with the Treaty on the Functioning of the European Union, which prohibits the monetary financing of countries via purchases of debt instrument issued by governments or public entities in the EU on the primary market, i.e. directly from the issuer. The eligible counterparties for the SMP are those that may participate in Eurosystem monetary policy operations and those that are used by a Eurosystem central bank for the management of its own euro-denominated investments.

The SMP focuses on those securities markets that were particularly adversely affected by the fiscal difficulties in individual euro area countries. Figure 1 illustrates the cumulative bond purchases under the SMP programme until the end of 2010.

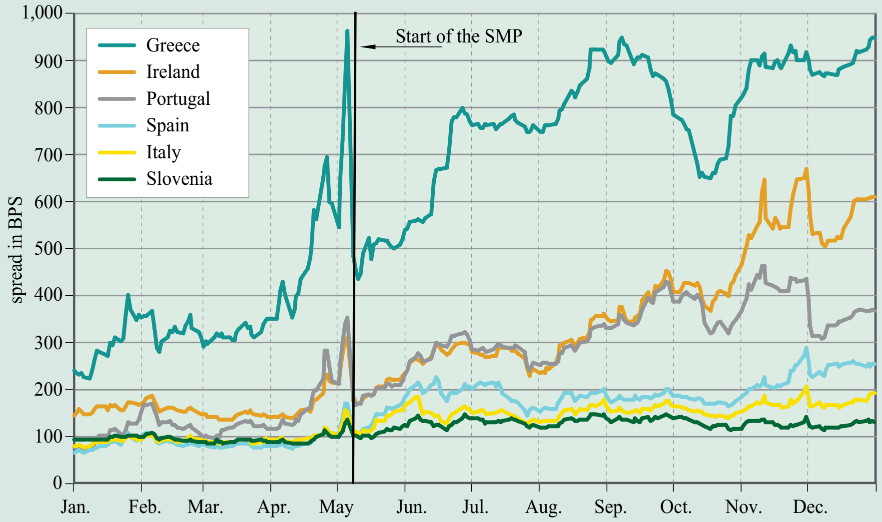
Figure 1: **Cumulative bond purchases under the SMP programme until the end of 2010**



Source: ECB

Figure 2 illustrates the yield spreads of certain euro area long-term government bonds over the benchmark German government bonds in 2010. The countries illustrated are those whose bonds had the highest and most volatile spreads. The figure shows that the spreads of the countries in question declined significantly when the SMP was announced, before gradually rising again. The spreads of 10-year Slovenian government bonds are shown for comparison; they have been stable since May, albeit at a slightly higher level.

Figure 2: **Spreads of 10-year government bonds of selected euro area countries over the German benchmark in 2010**



Source: Bloomberg Plc

A decline in lending in US dollars and Swiss francs.

Between December 2007 and the end of January 2010 the Eurosystem lent US dollars to European banks in cooperation with the Federal Reserve. In May 2010 this lending was reintroduced via weekly tenders with full allotment as a loan available to banks should they fail to find any other funding, i.e. at an interest rate above the market rate. The average loan amount was negligible. No Slovenian bank or savings bank participated in these tenders.

Similarly, between the end of 2008 and the end of January 2010 Swiss francs were lent to European banks in foreign exchange swaps. Because demand declined, the foreign exchange swaps were discontinued at the end of January 2010. The average daily amount of euro/Swiss franc foreign exchange swaps in January 2010 stood at EUR 1.3 billion, and at EUR 0.4 million at Slovenian banks and savings banks.

Standing facilities and minimum reserves

Daily use of the deposit facility in 2010 as a result of excess liquidity.

Since mid-October 2008, when the Eurosystem began using full allotment in its lending operations, banks have used the *deposit facility* on a daily basis to deposit excess liquidity. In 2010 the average daily balance of the deposit facility was EUR 145.9 billion, compared with EUR 109.4 billion in 2009. As is evident from Figure 21, as the 1-year LTROs started to mature the level of the deposit facility began to gradually decline. The use of the deposit facility by Slovenian banks and savings banks was similar to that of the euro area overall. Average use over 2010 was EUR 369 million, compared with EUR 356 million in 2009. Euro area banks made limited use of the marginal lending facility in 2010, averaging EUR 0.7 billion per day (compared with a daily average of EUR 0.9 billion in 2009), and never more than EUR 5.2 billion on any single day. The marginal lending facility was used only once in Slovenia in 2010.

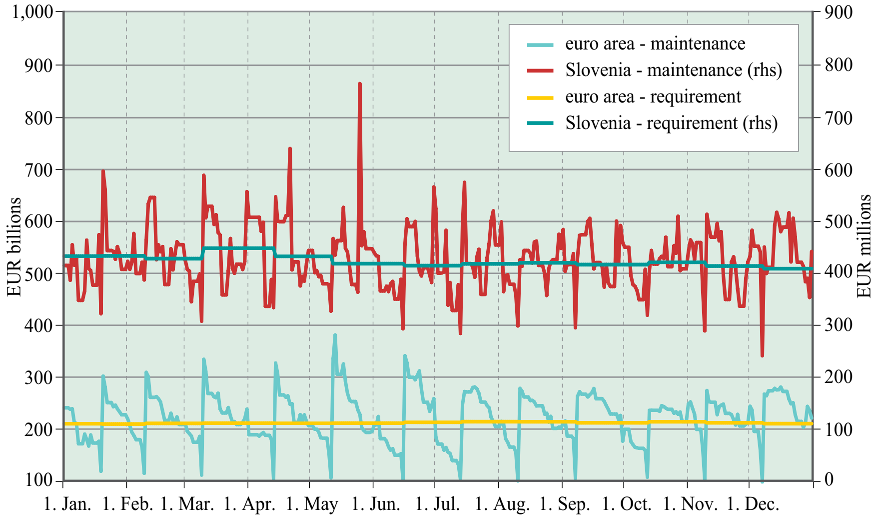
A decline of 2% in the minimum reserve requirement.

The Eurosystem's *minimum reserve system* comprises 2% of the amount of the reserve base on the liability side of the banks' balance sheets. [10] In 2010, the average reserve requirement in the euro area was EUR 211.9 billion (EUR 424 million in

[10] The Eurosystem's minimum reserve system is described in Chapter 7 of the General Documentation on Eurosystem Monetary Policy Instruments and Procedures, available at http://www.ecb.int/pub/pdf/other/gendoc2008en.pdf.

Slovenia), down 2.0% on 2009 (down 0.9% in Slovenia). The holdings used to meet the requirement averaged EUR 213.8 billion in 2010 for the euro area overall, and EUR 428 million in Slovenia. The difference is the desired excess reserves.

Figure 23: **Minimum reserve requirement and maintenance**



Sources: Bank of Slovenia, ECB

Collateral in Bank of Slovenia credit operations

In accordance with the Statute of the ESCB and of the ECB, all Eurosystem credit operations related to monetary policy and intraday loans must be secured (collateralised) by eligible assets. These must meet criteria that are the same throughout the euro area. Eligible assets are divided into marketable assets (debt securities) and non-marketable assets (primarily credit claims).[11]

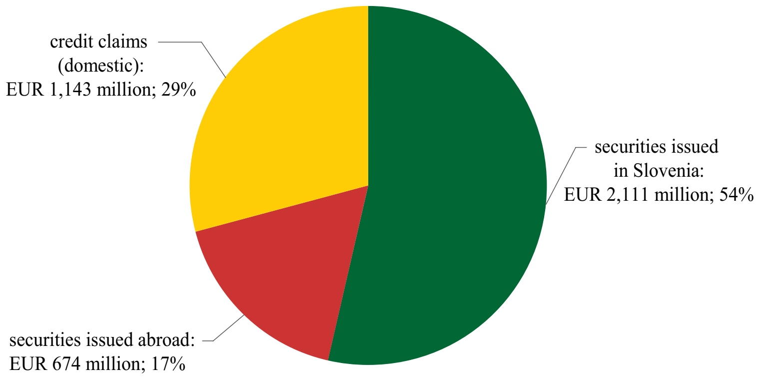
Due to increased borrowing by banks, the Eurosystem amended certain criteria for eligible collateral back on 15 October 2008. The collateral expansion was meant to be temporary, lasting until the end of 2009. Thus, in addition to existing collateral, the following were also made eligible: (a) securities (with the exception of asset-backed securities) and non-marketable assets with a credit rating between BBB+/Baa1 and BBB-/Baa3; (b) debt securities issued by credit institutions that are traded on certain OTC markets, as defined by the ECB; (c) subordinated debt securities with an eligible guarantee; and (d) certain debt instruments issued in the euro area and denominated in US dollars, pound sterling or Japanese yen. On 7 May 2009 the Eurosystem extended the aforementioned measures until the end of 2010. Then on 8 April 2010, as one of the responses to the sovereign debt crisis, it extended the measure under point (a) indefinitely, together with the announcement of the introduction of graduated, credit rating-dependent haircuts, which are to be applied from 1 January 2011 onward in determining the value of these eligible assets. As a result of the adoption of the programme to reduce the fiscal deficit and structural changes, on 3 May 2010 the application of the ratings threshold (i.e. ratings of BBB–/Baa3) in the assessment of the eligibility of securities issued or guaranteed by the Greek government was withdrawn.

11 Eligible assets are described in Chapter 6 of the General Documentation on Eurosystem Monetary Policy Instruments and Procedures, available at http://www.ecb.int/pub/pdf/other/gendoc2008en.pdf (see also Guideline of the European central bank ECB/2000/7 on monetary policy instruments and procedures of the Eurosystem with amendments, particularly Guideline ECB/2010/13).

The pool of collateral at the Bank of Slovenia remained high.

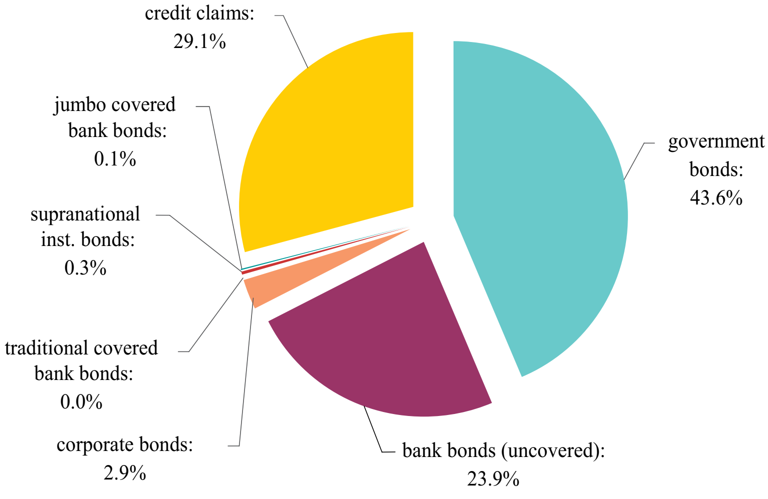
Slovenian banks and savings banks provide collateral to the Bank of Slovenia by transferring it to the pool of collateral at the Bank of Slovenia. Assets issued, deposited or settled in Slovenia are transferred to the pool by pledging eligible securities held at the Central Securities Clearing Corporation (KDD) or by entering in the register of bank loans at the Bank of Slovenia a lien on a bank loan. Assets issued abroad are transferred to the pool via the correspondent central banking model (CCBM).[12] After increasing in 2009, the pool of collateral remained relatively stable in 2010, fluctuating between EUR 3.8 billion and EUR 4.1 billion. It stood at EUR 3.9 billion at the end of the year, of which EUR 2.1 billion comprised securities issued in Slovenia, EUR 0.7 billion securities issued abroad, and EUR 1.1 billion domestic bank loans. Slovenian banks and savings banks began using domestic bank loans in December 2008, but did not use bank loans granted to borrowers abroad.

Figure 24: **Pool of collateral at the Bank of Slovenia as at 31 December 2010: breakdown by place of issue**



Source: Bank of Slovenia

Figure 25: **Pool of collateral at the Bank of Slovenia as at 31 December 2010: breakdown of securities by type and bank loans**



Source: Bank of Slovenia

The Bank of Slovenia is actively participating in the introduction of the new system for managing collateral for central bank claims, CCBM2 (Collateral Central Bank

12 The correspondent central bank model (CCBM) is a mechanism between Eurosystem central banks that permits counterparties to secure Eurosystem claims with financial assets issued or settled in a country other than the counterparties' country of origin. More information about the CCBM is available in an English-language brochure on the ECB's website at http://www.ecb.int/pub/pdf/other/ccbm2008en.pdf.

Management). This will be based on a standardised technical platform, which will be jointly owned by the central banks of the Eurosystem. The platform is being created to ensure greater technical and cost efficiency and to harmonise the functioning of central bank back-office operations for monetary policy lending. But most of all, it will enable euro area banks to access the collateral via a standardised system.

2.1.3 Bank of Slovenia as a lender of last resort

Article 4 of the Bank of Slovenia Act states that one of the Bank of Slovenia's objectives is to strive to ensure financial stability. On the basis of point 14 of Article 12 of the aforementioned law, the Bank of Slovenia may therefore act as the lender of last resort, i.e. in exchange for appropriate collateral it lends to a solvent bank or savings bank that could find itself in sudden liquidity difficulties. The Bank of Slovenia did not approve any such loans in 2010.

2.1.4 Payment and settlement systems

Payment and settlement systems are a vital part of the financial infrastructure of market economies, as their secure and efficient functioning allows for the reliable, timely and cost-effective settlement of financial transactions, most notably transactions arising in the execution of monetary policy by the central bank. Because they contribute to the general stability and efficiency of the economy, payment and settlement systems are a vital part of the economic and financial infrastructure. The Bank of Slovenia, as the central bank, therefore acts in several roles with regard to payment and settlement systems: it ensures the stability of individual payment system participants, it oversees the security and efficiency of payment and settlement systems; and it manages a payment system that facilitates the settlement of transactions in central bank money. Also of importance is its role as a catalyst and promoter of the activities of market participants, with the aim of improving competition and promoting development. Notwithstanding, in which of the before mentioned roles the Bank of Slovenia acts, its objective is to ensure transparent functioning and the clarity of its basic guidelines for all payment and settlement system participants.

TARGET2

TARGET2 is the pan-European payment system that allows the prompt settlement of individual payments. It is operated overall by the Eurosystem, and operates on a single joint technological platform, but in formal legal terms each central bank included in TARGET2 operates its own national component. The Slovenian component is called TARGET2-Slovenija.

An upgrade of the TARGET2 payment system was made in November 2010.

An update of the *General Conditions for Participation in TARGET2-Slovenija*.

Within the framework of Eurosystem activities the development of the functionality of the TARGET2 payment system continued in 2010. An upgrade was made in November that included modifications to the TARGET2 technological platform for the planned establishment of the new system for managing central bank collateral and modifications that allow participants to access the payment system online. The Bank of Slovenia organised testing for all TARGET2-Slovenija participants in connection with the upgrade. The aim was to allow participants in the payment system to test whether their own technological support required for the upgrade was adequate. In keeping with these upgrades the Bank of Slovenia also updated the *General Conditions for Participation in TARGET2-Slovenija*.

A proposal for the introduction of the ISO 20022 reporting standard was also drafted at the Eurosystem level. The discussion of this proposal with TARGET2 participants proceeded in Slovenia within the framework of the TARGET2 National User Group, which operates under the aegis of the Bank of Slovenia. On the basis of the responses of all participants, a strategy for the introduction of the ISO 20022 to the TARGET2 payment system was drawn up in December 2010. In line with this strategy the standard will be introduced in three steps, in the years 2013 to 2015.

In connection with the further development of the TARGET2 payment system, preparations were also made in 2010 within the framework of the Eurosystem for the next major upgrade to the technological platform, which is projected for November 2011.This upgrade will mainly introduce modifications to improve the interface via which participants monitor transactions in the payment system. Discussion of the details of this upgrade – the framework was finally determined in December 2010 – also proceeded within the TARGET2 National User Group.

TARGET2-Securities

Creation of centralised infrastructure for securities settlement.

TARGET2-Securities (T2S) is a Eurosystem project to set up a single technical platform for the settlement of transactions in securities in a way that will entail assuming the function of securities settlement from European central securities depositories, and centralising settlement together with cash accounts on a single platform operated by central banks. The primary aim of T2S is to consolidate securities settlement infrastructures in the EU, which are currently fragmented and locally oriented, thus increasing the effectiveness and security of securities settlements, and ultimately improving the global competitiveness of European securities markets. The decision to build T2S was taken in July 2008, with the central banks of France, Italy, Germany and Spain responsible for the construction and operation of the platform.

Preparations of detailed user functional specifications as the key technical documentation for the functioning of T2S and as a guarantee of compatibility between the central securities depositories and T2S were made at the Eurosystem level in 2010. There was also activity in the areas of drafting the binding contractual relations regarding the use of T2S between individual participants (the key stakeholders are the Eurosystem, the central securities depositories and the central banks outside the Eurosystem), updating the project management structure for the phase of setting up T2S, and defining the costs of construction and operation and the T2S pricing policy. The key decisions of the Governing Council of the ECB in 2010 related to the deadline for the construction of T2S being moved to September 2014, to the approval of the T2S Guidelines, and to the approval of the costs of construction and operation and of transaction prices. The criteria for selecting bidders for the communications network for accessing T2S were also drawn up.

The Bank of Slovenia maintains an active dialogue within the T2S National User Group.

The Bank of Slovenia's activities in the area of T2S encompassed participation at the Eurosystem level and activities in the national environment. In the national environment the Bank of Slovenia maintains an active dialogue with Slovenian market participants within the framework of the T2S National User Group, whose primary task is to design the most effective way of integrating the Slovenian environment into T2S. Activities proceed on the basis of an analysis of the T2S technical documentation and identification of the requisite modifications in the environment of the Central Securities Clearing Corporation (KDD), the Bank of Slovenia and other market participants. At the same time within the group there is a broad exchange of information and opinions in connection with the T2S project, and the commentary and positions of the national environment are drawn up as part of consultations within the Eurosystem.

Preparation of a model for the integration of the CSCC into T2S.

In narrow terms T2S will entail the imposition of harmonised technical and legal requirements vis-à-vis European central securities depositories in various areas (technical access, range and level of services, pricing policy, governance, changes in functionality, etc.). Modifications will therefore be necessary in all national environments. The extent of the modifications depends on the discrepancy between the envisaged manner of operation of T2S and the current market practices in the individual national environments. In this context the Bank of Slovenia worked intensively with the KDD in 2010 to draw up a technical model for the integration of the KDD into T2S, which together with elements of the contractual relationship between the Eurosystem and the KDD will form the basis for the KDD's decision regarding its participation in T2S. Subsequently the model will form the basis for the preparation of detailed technical documentation of internal modifications at the KDD and also in part at the Bank of Slovenia. At the same time there was also a process of identifying urgent legal amendments to establish a stable legal framework for the continuation of the KDD's work on the implementation of a technical solution. Activities to amend legislation thus commenced in October in conjunction with the Bank of Slovenia, the KDD, the Ministry of Finance and the Securities Market Agency. In addition the Bank of Slovenia began preparing an analysis of the requisite internal modifications. These will be vital because of the assumption of the function of managing cash accounts of Slovenian participants in T2S, which will require specific changes to the structure of the cash accounts of members of the KDD, which are already managed by the Bank of Slovenia.

Collateral Central Bank Management (CCBM2)

Creation of a standard technical platform for Eurosystem collateral management.

The Collateral Central Bank Management (CCBM2) is a Eurosystem project to build a standard, cost-efficient technical platform for managing the collateral used for all credit operations of Eurosystem central banks.

In line with the principle of decentralisation, central banks will continue to carry out their tasks in the national environment, while existing technical support relating to the management of credit operations may be outsourced to CCBM2. The technological design of the platform will be based on a modular architecture, from which each participating central bank will select the functionality of the platform based on its own needs and those of the national environment.

The functional framework of CCBM2 will allow for the provision of basic services in the management of domestic and cross-border eligible collateral (transactions and custody) in real time. It will also provide support for all central depository corporation services, which are aimed at the more efficient use of available collateral of market participants (triparty collateral management services) and for auto-collateralisation services. Interoperability of CCBM2 with the TARGET2 payment system and the planned TARGET2-Securities settlement system platform will also be ensured.

Participation in the CCBM2 project within the framework of Eurosystem working bodies.

The Bank of Slovenia's activities in the area of CCBM2 in 2010 encompassed intensive cooperation in the creation of detailed project technical documentation within the framework of Eurosystem working bodies. Further wide-ranging activities were related to the creation of a harmonised legal basis, testing strategies and the changeover to the use of CCBM2, security policy and the most effective way of ensuring interoperability between CCBM2 and other Eurosystem projects. On this basis a concept for the integration of the Bank of Slovenia and its counterparties into CCBM2 was drawn up, approved and adopted subject to national specifics in the arrangements of the execution and collateralisation of Bank of Slovenia credit operations.

Single euro payments area (SEPA)

In the SEPA project the Bank of Slovenia acts as a catalyst and promoter of change.

The aim of the establishment of the Single Euro Payments Area (SEPA) is to create an integrated European payments market in euros, in which effective competition will be established and the distinction between domestic payments and cross-border payments would be abolished. The establishment of SEPA in Slovenia is managed by the Bank Association of Slovenia (BAS), which is also a member of the European Payments Council (EPC).

With the fulfilment of the requirement for interoperability for SEPA cross-border direct debits on 1 November 2010, in accordance with *Regulation (EC) No. 924/2009 of the European Parliament and of the Council of 16 September 2009 on cross-border payments in the Community and repealing Regulation (EC) No. 2560/2001* Slovenian payment service providers have offered a pan-European payment instrument that allows Slovenian consumers and companies to pay liabilities in accordance with the SEPA direct debit scheme within the country and across borders throughout SEPA. In the gradual changeover from national legacy credit transfers to already launched SEPA credit transfers, an important milestone was the introduction of the universal payment order (also on 1 November 2010), which will gradually replace the old credit transfer forms.

Active participation in SEPA project working bodies under the aegis of the BAS.

Also in 2010 the Bank of Slovenia actively participated in the working and support groups of the SEPA project and in the National SEPA Implementation Committee, which operate under the aegis of the BAS. Within the aforementioned committee the Bank of Slovenia has the opportunity to present its views and to influence the adoption of key decisions regarding the implementation of SEPA in Slovenia. The Bank of Slovenia's active participation in the working and decision-making bodies within the SEPA project provides the requisite basis for the execution of its tasks. As part of the Eurosystem the Bank of Slovenia also supports the SEPA project at the national level, and acts as a catalyst and promoter of change. Here its primary tasks relate to the coordination and guidance of the banking sector's activities in accordance with the Eurosystem policy. The Bank of Slovenia also expresses its support for the SEPA project within the framework of the National SEPA Forum, which was revived in early 2010 and offers an opportunity for dialogue between providers and users of payment services. One of the Bank of Slovenia's key tasks within the framework of the National SEPA Forum is to contribute to building a positive image of SEPA, thereby indirectly encouraging stakeholders to mitigate to already implemented SEPA solutions at the earliest possible juncture.

Monitoring of progress in the changeover to the use of SEPA payment instruments.

The Bank of Slovenia's activities regarding SEPA in 2010 also encompassed the regular monitoring of progress in the establishment of SEPA in Slovenia, in relation to SEPA credit transfers, SEPA direct debits and SEPA card payments. Each month the Bank of Slovenia announces the progress in the changeover to the use of SEPA credit transfers in Slovenia (at the level of payment systems) on its website.

In 2010 a great deal of attention, particularly in terms of assessing the impact on the Slovenian environment, was devoted to the content of the nascent European Commission regulation, the primary purpose of which is to accelerate and complete the changeover to the use of pan-European payment instruments. It alters the nature of the SEPA project from one of self-regulation to a project that is supported with vital legislative measures. When it enters into force certain elements of the regulation will also have an impact on the Slovenian banking sector, on payment service users, and also on the Bank of Slovenia as the provider of payment services for the state and local government and its other clients.

SEPA infrastructure management and the settlement function

Provision of cross-border availability in SEPA credit transfer and SEPA direct debit schemes.

The Bank of Slovenia ensures a link between the systems, which are operated by Bankart d.o.o., for the execution of (primarily cross-border) SEPA credit transfers and SEPA direct debits to the pan-European payment systems for these payment instruments operated by EBA Clearing. As a direct participant in pan-European payment systems, the Bank of Slovenia allows banks and savings banks in Slovenia to exchange SEPA credit transfers with almost 4,500 payment service providers around Europe. By providing the link, which was established on 1 November 2010 for SEPA direct debits, the Bank of Slovenia ensures the cross-border reachability of bank accounts in Slovenia for SEPA direct debits. This has allowed banks and savings banks to meet the requirements deriving from *Regulation (EC) No. 924/2009 of the European Parliament and of the Council of 16 September 2009 on cross-border payments in the Community and repealing Regulation (EC) No. 2560/2001.*

Settlement in risk-free central bank money.

In 2010 the Bank of Slovenia also acted as the settlement agent for the SEPA Internal Credit Transfers payment system, ATM Settlement and Card Settlement payment systems (operated by Bankart d.o.o.), Activa Multilateral Clearing (operated by Banka Koper d.d.) and MasterCard Multilateral Clearing (operated by MasterCard International). This means that it ensures that the claims and liabilities of participants in these payment systems are settled in their accounts held at the Bank of Slovenia in risk-free central bank money.

Payment and settlement systems oversight

Oversight of payment and settlement systems is a central bank function. The aim of the process of monitoring, analysing and guiding changes (also by taking action in the event of a payment and settlement system failing to meet the prescribed requirements and standards) is to ensure security and efficiency in payment and settlement systems, thereby contributing to ensuring systemic stability, mainly to reduce systemic risk and maintain public confidence in these systems.

Oversight of payment and settlement systems operations.

On the basis of the *Bank of Slovenia Act* and the *Payment Services and Systems Act,* the Bank of Slovenia is competent and responsible for overseeing payment systems operations. Also serving as the basis for oversight is the *Regulation on payment systems*, which was adopted on the basis of the *Payment Services and Systems Act*. The regulation sets out detailed rules for the criteria for defining a systemically important payment system, requirements for managing financial, operational and other risks in payment systems, and for reporting on the operations of payment systems. When conducting oversight the Bank of Slovenia also follows the guidelines of the Eurosystem and the *Core Principles for Systemically Important Payment Systems*,[13] which were approved by the Governing Board of the Bank of Slovenia as the basis for oversight.

In 2010 the Bank of Slovenia, in accordance with its responsibilities, oversaw the operations of payment systems on the basis of analysis of regular and ad hoc reports of payment system operators in Slovenia, which are obliged to submit such reports to the Bank of Slovenia. The operators' reports relate to the regular operations of the systems and the operations of payment system operators, all planned or unplanned deviations from regular operations, as well as changes in the functional concept of payment systems operations. The Bank of Slovenia also monitored the implementation of measures imposed on payment system operators on the basis of on-site oversight of payment systems and their operators.

[13] Core Principles for Systemically Important Payment Systems, Committee on Payment and Settlement Systems (Bank for International Settlements), 2001.

The Bank of Slovenia also participated in activities carried out at the Eurosystem level with regard to payment systems, payment schemes and important payment system infrastructures oversight. These activities primarily include the preparation of standards and methodologies for conducting oversight of payment systems, links between payment systems and payment schemes and cooperative oversight of pan-European payment systems, payment schemes and important payment system infrastructure with participants from various countries.

Participation in examinations at the Eurosystem level.

Another important function of central banks is the oversight of the development and functioning of securities settlement systems. These represent an important element of the infrastructure of every securities market, as they ensure compliance with the obligation to transfer and settle securities. A keen interest of central banks is therefore the smooth functioning of and effective risk management in these systems, as possible weaknesses can be a source of financial and operational risks for the participants in these and other related securities settlement and payment systems. The Bank of Slovenia is competent and responsible for overseeing the functioning of securities settlement systems on the basis of the *Bank of Slovenia Act*, while this responsibility is further reinforced by the *Financial Instruments Market Act*, which imposes the authority and responsibility for the oversight of the central securities depository, in terms of systemic risk in the settlement system, on the Bank of Slovenia. The Bank of Slovenia cooperates with the Securities Market Agency in this regard. A number of consultations between the Bank of Slovenia and the Securities Market Agency were held in this context in 2010.

Within this function a place is also being given to the activity of assessing the compliance of the functioning of the KDD with the requirements of the Eurosystem as a user of KDD services. Assessment of the KDD's compliance with the *Standards for the use of securities settlement systems in Eurosystem credit operations* and the KDD's existing links with foreign central securities depositories (Clearstream Banking Frankfurt and Clearstream Banking Luxembourg) began in December 2010.

Start of user assessment of the CSCC with regard to Eurosystem requirements.

Here within Eurosystem working bodies the Bank of Slovenia was also involved in the creation of European legislation on clearing and electronic registers of transactions in financial derivatives, which will be finalised in 2011 in the form of the European market infrastructure regulation. Monitoring of European Commission initiatives to draw up principles for future regulation of central securities depositories also proceeded at the same time.

Oversight of payment institutions

Under the *Payment Services and Systems Act*, payment institutions are newly recognised as independent providers of financial services, and are therefore an important and potentially critical part of the financial system.

Payment institutions newly recognised as independent providers of financial services.

Given the nature of the services that they provide, payment institutions are required to operate securely and reliably. To this end they must manage operational and financial risks. This means that they should be organised as one of the legal corporate forms, the suitability of holders of qualifying holdings in the institution should be ensured, organisational, personnel and technical conditions should be met, and an adequate level of capital and appropriate security of users' money should be maintained at all times.

The Bank of Slovenia is competent and responsible for overseeing payment institutions.

Payment institutions can only provide individual payment services if they have obtained prior authorisation from the Bank of Slovenia in accordance with the *Payment Services and Systems Act*, while their operations are subject to constant oversight. The Bank of Slovenia is competent and responsible for issuing authorisations and for overseeing whether payment institutions meet the conditions.

Within the framework of its handling of payment institutions, in 2010 the Bank of Slovenia mainly put in place organisational, personnel and technical conditions for the comprehensive implementation of its new oversight function. The conditions were put in place for discharging the competencies and responsibilities set out in the *Payment Services and Systems Act*, which include the issuing, rejection, expansion and revocation of authorisations and the administration of a public register of payment institutions accessible on the Bank of Slovenia's website. At the same time the conditions were also put in place for conducting oversight of payment institutions by means of monitoring, collecting and reviewing of their reports, on-site overseeing of payment institutions and cooperating with other supervisory authorities responsible for overseeing payment services in Slovenia and in EEA Member States.

A major feature of the activities in the oversight of payment institutions in 2010 was the provision of the *Payment Services and Systems Act* that provides for a transitional period for obtaining the authorisation to provide payment services for those payment service providers that were already providing services before 25 December 2007 (these providers are obliged to obtain the Bank of Slovenia authorisation to provide payment services by 30 April 2011). The transitional period applies to the majority of identified payment institutions, which have made use of for the demanding process of preparing and submitting the application for obtaining the authorisation. For the Bank of Slovenia this meant that it only began receiving applications for the issuing of authorisations at the end of 2010.

Identification of potential payment institutions.

During 2010, i.e. before applications for the authorisation were submitted, some payment services providers merely made enquiries at the Bank of Slovenia as to their status and their legal requirements vis-à-vis the bank. Here, based on information from the business environment, the Bank of Slovenia itself also actively undertook the identification of those payment service providers that would be obliged to obtain the authorisation to provide payment services as a payment institution and that had not yet made enquiries about their status.

Payment services in Slovenia may also be provided by payment institutions of EEA Member States, either via a branch, via an agent, or directly, whereby the Bank of Slovenia is notified by the relevant supervisory authority of the payment institution’s home country (notification of payment institutions). By the end of 2010 the Bank of Slovenia had received more than 40 notifications from foreign supervisory authorities in connection with the provision of payment services in Slovenia either directly or via agents. The vast majority of the notifications were made by the supervisory authorities of the UK and Ireland, most often in relation to the direct provision of money remittance services. The list of notified payment institutions of EEA Member States is published by the Bank of Slovenia on its website.

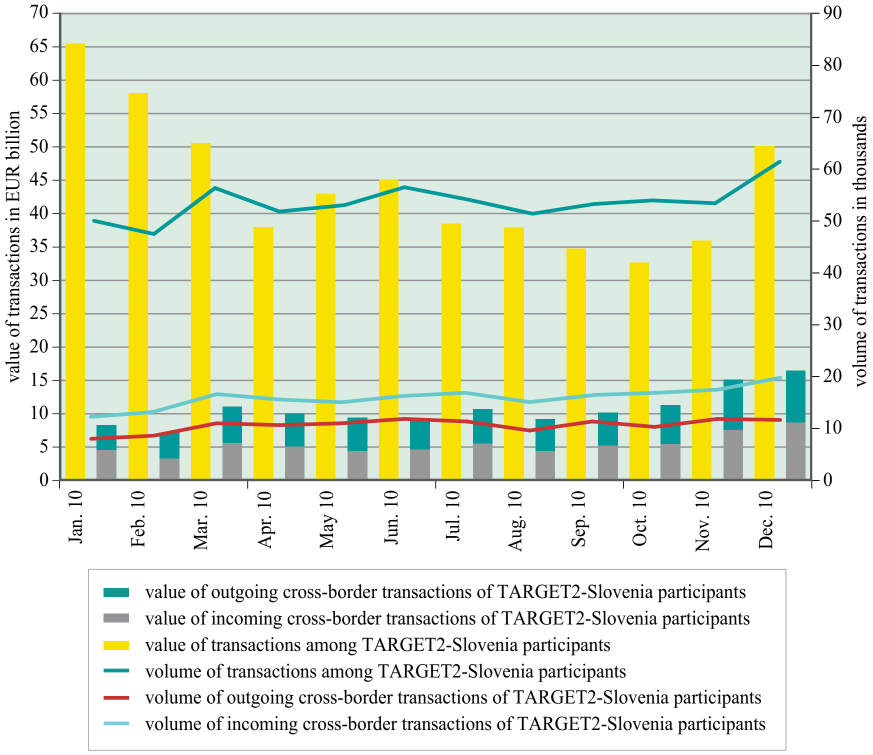
Statistics for payment systems operated by the Bank of Slovenia

The Bank of Slovenia operates the TARGET2-Slovenija system for the settlement of high-value and urgent payments in euros.

In 2010 there were 647,231 transactions settled between participants in the TARGET2-Slovenija payment system with a total value of EUR 530,107.17 million, a decline of 3.02% in the number of transactions and an increase of 4.43% in the value of transactions compared to 2009. Between participants in the TARGET2-Slovenija system and participants in other national components of the TARGET2 system 191,219 incoming cross-border transactions were settled, up 11.56% compared to 2009, with a total value of EUR 64,692.57 million, up 0.76% compared to 2009, and 127,269 outgoing cross-border transactions, up 8.42% compared to 2009, with a total value of EUR 63,440.59 million, down 0.84% compared to 2009.

The value of transactions between TARGET2-Slovenija participants was up 4.43%, while the number of transactions was down 3.02% compared to 2009.

Figure 26: **Number and value of transactions via the TARGET2-Slovenija system by month in 2010**



Source: Bank of Slovenia

2.1.5 Joint management of the ECB's foreign reserves

With the adoption of the euro on 1 January 2007, the Bank of Slovenia transferred its portion of foreign currency assets in US dollars and gold to the ECB. The main purpose of the international monetary reserves is to ensure adequate liquidity for operations on the currency market. All euro area central banks have contributed their shares to the ECB's foreign reserves, which they manage jointly with the ECB. Since 1 January 2007 the Bank of Slovenia and the Central Bank of Luxembourg have jointly managed their share of the ECB's international monetary reserves. In addition to the international monetary reserves transferred to the ECB, the Bank of Slovenia also holds a portion of its investments in foreign currency in case the ECB calls for additional monetary reserves, which is in accordance with Article 30 of the Protocol on the Statute of the European System of Central Banks and the European Central Bank (see also section 2.2.3).

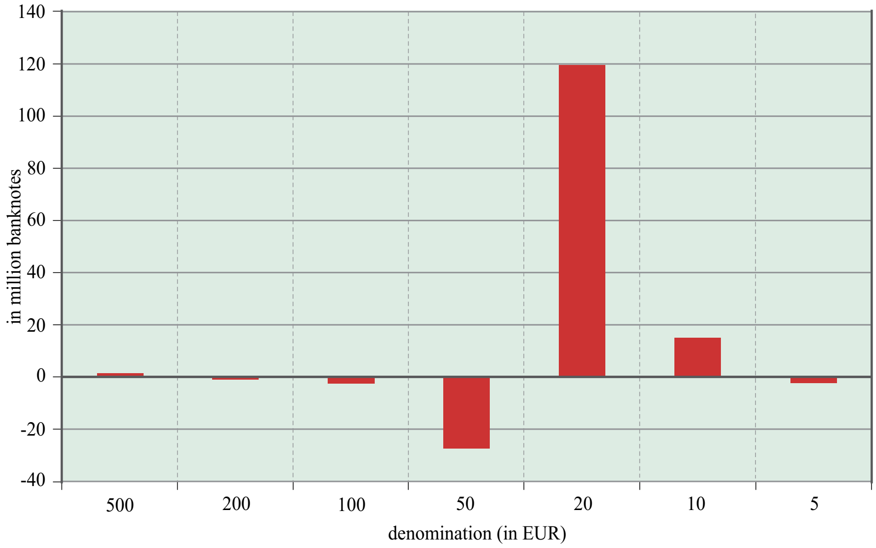
2.1.6 Cash operations

The Bank of Slovenia has issued a net total of EUR 1.21 billion in cash since the introduction of the euro in 2007.

A net total of EUR 1.21 billion of cash had been released into circulation via the Bank of Slovenia by the end of 2010, of which banknotes accounted for EUR 1.17 billion (103.19 million banknotes), and coins for EUR 45.59 million (173.18 million coins). In terms of quantity, the EUR 20 note was the most heavily issued (119.57 million banknotes), followed by the EUR 10 note (14.83 million banknotes) and the EUR 500 note (0.63 million banknotes). For all other denominations (EUR 200, EUR 100, EUR 50 and EUR 5), the number of banknotes issued was lower than the number returned to the Bank of Slovenia. The coins that were issued most heavily in terms of net quantity were the 1-cent (44.28 million coins) and 2-cent (34.98 million coins), while the lowest net quantity of issued coins was recorded by the EUR 1 (6.45 million coins).

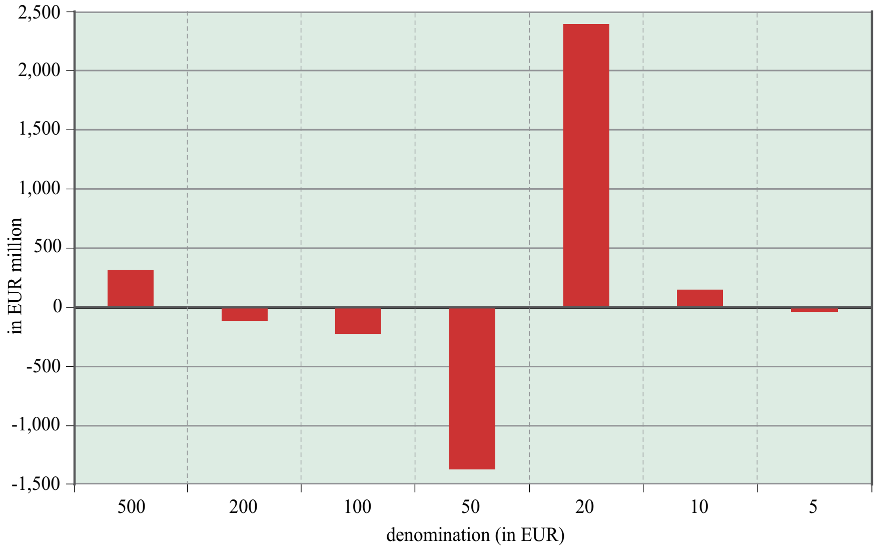
The Bank of Slovenia organised the issue, distribution and storage of general circulation and commemorative coins for the Republic of Slovenia.

Figure 27: **Quantitative breakdown of net issued euro banknotes after entry into the euro area**



Source: Bank of Slovenia

Figure 28: **Value breakdown of net issued euro banknotes after entry into the euro area**



Source: Bank of Slovenia

In May 2010 the Bank of Slovenia released 1,000.000 new commemorative EUR 2 coins into circulation to mark the 200th anniversary of the Botanic Gardens in Ljubljana. Collector coins issued by Slovenia were made available for sale and released into circulation by the Bank of Slovenia to mark the world ski flying championships at Planica (5,000 gold coins and 7,000 silver coins) and to commemorate Ljubljana as World Book Capital 2010 (4,000 gold coins, 6,000 silver coins and 300,000 bi-coloured EUR 3 collector coins).

Commemorative coins issued in 2010.

For the collector market the Bank of Slovenia issued a collection of euro coins minted in 2010, a card with a commemorative EUR 2 coin and a card with a EUR 3 collector coin.

As at 31 December 2010 there remained in circulation 46.90 million tolar banknotes (worth SIT 7.99 billion), 445.81 million tolar coins (worth SIT 2.17 billion), and 20.92 million payment notes (worth SIT 404.14 million). Compared with circulation at the end of 2005, of the tolar banknotes 58.6% pieces have been returned from circulation, or 96.3% of the total value of tolar banknotes, and 13.5% of the tolar coins, or 37.4% of the total value of tolar coins.

The total value of tolar banknotes, coins and payment notes still in circulation is EUR 44.08 million.

The payment notes and tolar banknotes are exchangeable at Bank of Slovenia counters with no time limit, while coins must be exchanged by 31 December 2016.

The payment notes, tolar banknotes and tolar coins are exchangeable at the Bank of Slovenia.

A total of 5,452 treasury receipts and outlays of euro cash (2009: 9,686) and 3,949 incoming and outgoing payments of cash for the needs of government bodies were made in 2010 (2009: 5,152), as were 4,122 exchanges of tolar banknotes and coins.

The Bank of Slovenia cash processing unit sorted 79.0 million banknotes and coins (2009: 41.19 million), comprising 38.64 million banknotes and 40.36 million coins (2009: 34.63 million banknotes and 6.56 million coins). A total of 10.8 million banknotes (compared with 16.77 million banknotes in 2009) were taken out of circulation and destroyed in order to maintain an appropriate quality of banknotes in circulation.

79.0 million banknotes and coins were sorted at the Bank of Slovenia cash processing unit.

Euro cash was supplied nationally via depots at banks.

The Bank of Slovenia ensured the supply of euro cash via its banknote depots at five commercial banks, reviewing their operations daily.

The expert committee for testing, verifying and setting up devices to process euro banknote and coin handling machines carried out 35 monitoring tests in 2010, by which it verified that the banknote handling machines at commercial banks were working accurately and properly. Based on the data obtained (the number and type of sorting systems), the Bank of Slovenia drew up a timetable for testing. It was appropriately taken into consideration that in Slovenia the majority of activities in connection with the fitness and authenticity of euro banknotes are carried out at the five Bank of Slovenia banknote depots (NLB, NKBM, Banka Celje, Gorenjska banka and Banka Koper), where most testing was also conducted. In 2010 all tests were successful.

The value of euro counterfeits increased.

According to the figures of the National Analysis Centre (NAC) and the Coin National Analysis Centre (CNAC), 2,603 counterfeit euro banknotes and 1,518 counterfeit euro coins were withdrawn from circulation in 2010, compared to 1,891 banknotes and 1,448 coins in 2009. In 2010, the number of counterfeit euro banknotes and coins in Slovenia increased: the number of banknotes by 37.6% and the number of coins by 4.8%. In the same year, the value of the counterfeits was EUR 746,323, compared to EUR 118,592 in 2009. The increase of 529.3% was the result of two major cases of counterfeiting. Without these the value would have been EUR 86,323, down 27.2% on 2009. EUR 500 notes accounted for the largest proportion of counterfeit banknotes in terms of quantity (51.1%), while EUR 2 coins accounted for largest proportion of counterfeit coins (63.1%). The number of counterfeit items redeemed at banks and shops in Slovenia has fallen slightly. Eurosystem data in this area ranks Slovenia in the lowest quartile of countries by the amount of counterfeit cash withdrawn from circulation per 1,000 inhabitants.

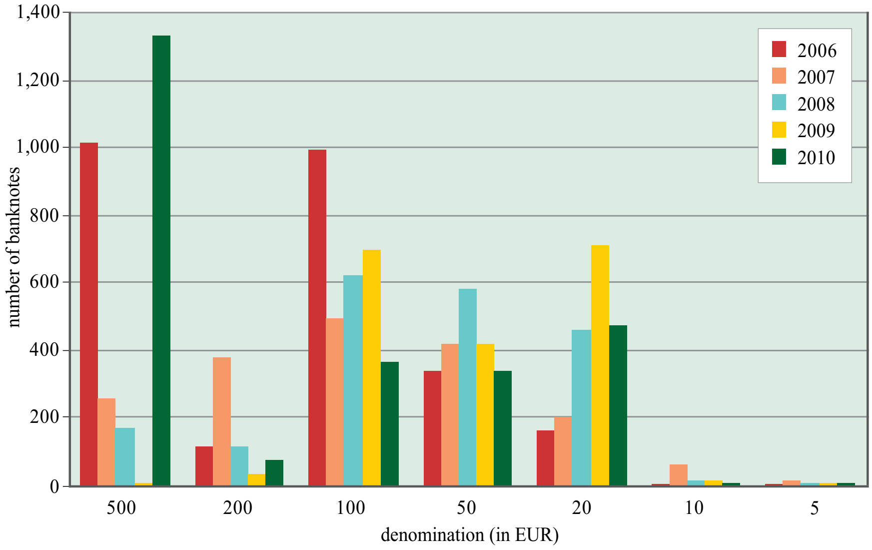
Counterfeits of foreign currency were also withdrawn from circulation.

In 2010, 138 foreign currency counterfeits (US dollars, Bosnian convertible marks) were withdrawn from circulation, compared with 61 in 2009. The quality of foreign currency counterfeits has improved over time, making it more difficult for users to identify them, particularly US dollar counterfeits.

Monitoring of the authenticity of euro cash was organised.

In line with Regulation (EC) No. 1338/01, the NAC and CNAC are responsible for issuing expert opinions on the authenticity of euro cash. These agencies operate within the Centre for Forensic Investigation (CFI) at the Ministry of the Interior. Supervision of the activities of the aforementioned centres, in connection with the work of the Counterfeit Monitoring System at the ECB, is carried out at the Bank of Slovenia by the National Counterfeit Centre (NCC). The NCC is actively involved in a system of data and information exchange on counterfeiting with the European Central Bank's Counterfeit Analysis Centre, other national counterfeit centres and the European Technical and Scientific Centre (ETSC) for the analysis of euro banknotes.

Figure 29: **Counterfeit euro banknotes discovered in Slovenia**



Source: Bank of Slovenia

2.1.7 Statistical system

The Bank of Slovenia is responsible for the implementation of integral statistical processes in monetary and financial statistics, the statistics of international relations and the statistics of the national financial accounts. This entails the collection and processing of data, its dissemination to users and/or the publication of aggregated data. The Bank of Slovenia also carries out certain tasks with regard to other economic and public finance statistics.

Responsibility for monetary and financial statistics, financial accounts statistics and international economic relations statistics.

The implementation of statistical functions is based on membership in the ESCB in accordance with the Statute of the ESCB and of the ECB, on the tasks of the statistical research programme under the National Statistics Act, and on other authorisations.

The Bank of Slovenia's statistical activities are used to inform the domestic and foreign public of the financial and macroeconomic trends in Slovenia, and also provide data support for the realisation of targets related to price stability, economic policy and the financial stability of the Slovenian economy within the framework of the EMU.

The Bank of Slovenia cooperates with international organisations and institutions, particularly the ECB, IMF, Eurostat (European Statistical Office within the European Commission), the World Bank, the BIS and the OECD on the development of statistical requirements, methodologies and standards. Bank of Slovenia representatives sit on the ESCB's Statistics Committee and the regular working groups for external statistics, general economic statistics, general government statistics, monetary and financial statistics, euro area (national) accounts, and statistical information systems, and also on occasional thematic groups such as the group for the development of the ESCB's central database of securities. The organisation of the Financial Statistics Department has been aligned with the need to cooperate within the ESCB.

Statistical cooperation within the framework of the ESCB and other international organisations and institutions.

Bank of Slovenia representatives also attend meetings of the relevant Eurostat working groups and regular plenary sessions of the Committee on Monetary, Financial and Balance of Payments Statistics (CMFB), which is the main body for coordinating strategic issues concerning European macroeconomic statistics for European central banks (including non-EU countries), statistical offices, Eurostat and the ECB.

The MoU with the Ministry of Finance and the SORS is the basis for meeting requirements in the area of macroeconomic and financial statistics.

The most notable form of cooperation with national statistical institutions is with the Ministry of Finance and the Statistical Office of the Republic of Slovenia (SORS), based on a Memorandum of Understanding in the area of macroeconomic and financial statistics, signed in 2004 and updated in 2009. The MoU was modelled on a document agreed between the ECB and Eurostat. It applies to the coordination of authorisations and responsibilities as a result of the increased burden of statistical requirements and co-dependency of particular statistics, thereby easing the fulfilment of international statistical requirements.

The MoU sets out the responsibilities of the signatories and the manner of their cooperation in the provision of Slovenian macroeconomic and financial statistics to the European Commission, Eurostat, ECOFIN, the ECB and the OECD. The MoU also covers cooperation in maintaining the register of standard classification of institutional sectors, which represent a particularly important statistical infrastructure for the provision of macroeconomic and financial statistics. The official sector classification is managed by the Agency for Public Legal Records and Related Services (AJPES) as part of the Business Register of Slovenia.

The main basic data source for the Bank of Slovenia is comprehensive and complex sets of financial accounts statistics, and monetary, financial and external statistics is data from direct and indirect reports from financial institutions and non-financial corporations and data on merchandise trade prepared by the SORS, in cooperation with the Customs Administration of the Republic of Slovenia. The Bank of Slovenia also collects, compiles and/or publishes statistics on payment instruments and financial markets, as well general economic and public finance statistics.

Compilation of financial accounts statistics on the basis of quarterly reports collected by AJPES.

The Bank of Slovenia compiles annual and quarterly financial accounts statistics on the basis of quarterly reports by institutional business units (non-financial corporations, financial corporations and government units) collected for the Bank of Slovenia by AJPES. In 2010 the Bank of Slovenia compiled quarterly financial accounts for the final quarter of 2009 and the first three quarters of 2010, as well as annual financial accounts for 2009.

Aggregate quarterly financial accounts statistics were submitted to the ECB in accordance with Guideline ECB/2005/13, while aggregates of quarterly financial accounts for the government sector were submitted to the ECB and Eurostat in accordance with Regulation (EC) No. 501/2004 and aggregates of annual financial accounts were submitted to Eurostat in accordance with Regulation (EC) No. 2223/96.

The publication Financial Accounts of Slovenia 2004-2009 was released in November 2010, and alongside tables of financial accounts and the compilation methodology it also contained analysis of aggregates in individual sectors, which for the first time included a comparison with the financial accounts of the euro area. In 2010 quarterly bulletins of the Financial Accounts of Slovenia for the third and fourth quarters of 2009 and the first and second quarters of 2010 were prepared and published on the Bank of Slovenia's website.

A new regulation on reporting data for financial accounts statistics was published in December 2010 (Official Gazette of the Republic of Slovenia, No. 102/2010); it amended the reporting threshold of units of S.11 from total assets of EUR 1 million to total assets of EUR 2 million.

Higher reporting threshold for non-financial corporations in financial accounts statistics.

The comprehensive production of monthly, quarterly and annual monetary and financial statistics continued in 2010 in accordance with the methodological requirements of the ECB, the BIS and the IMF, and the needs of the Bank of Slovenia. In addition to the balance sheet and interest rate statistics of monetary financial institutions (MFIs), the data pursuant to Regulations ECB/2001/13 and ECB/2001/18 and Guideline ECB/2007/9 also includes data on non-monetary financial intermediaries, securities, payment systems and structural data from the banking system.

In July 2010 other monetary financial institutions, with the exception of money-market funds, began reporting to the Bank of Slovenia using an updated, more detailed multi-purpose report. In addition to the requirements of the recast balance sheet regulation (ECB/2008/32) and interest rates regulation (ECB/2009/7), it includes the basic section of the unconsolidated prudential financial report (FINREP), the requirements of financial accounts statistics and international economic relations in connection with MFIs and other analytical needs of the Bank of Slovenia. These changes meant that the principle of multi-purpose reporting was thoroughly put into practice, thereby reducing the reporting burden on credit institutions in accordance with the recommendations adopted by the Governing Council of the ECB.

Updated multi-purpose reporting by credit institutions.

Bank of Slovenia Governor Marko Kranjec, Ph.D. gave a successful presentation of the Bank of Slovenia's experience with the multi-purpose reporting system in the context of the need for the flexible capture of data from financial intermediaries during the economic and financial crisis at the ECB statistics conference (held in Frankfurt on 19 and 20 October 2010).

Presentation of multi-purpose reporting at an ECB statistics conference.

In 2010 the Bank of Slovenia also initiated activities to introduce multi-purpose reporting of data in the subsector of insurance corporations and pension funds (S.125) in cooperation with the Insurance Supervision Agency (ISA) and the Slovenian Insurance Association (SIA).

Balance of payment and international investment position data, including external debt, FDI figures and international monetary reserves, were produced regularly in 2010.

As in every year, after the final data for merchandise trade for 2009 was received it was subject to a scheduled revision, which generally includes the figures for the last two years. Because in 2010 the SORS speeded up the revision of the merchandise trade figures compared with previous years, the Bank of Slovenia agreed to revise its figures by the end of July, two months earlier than in previous years. The revision was made earlier because of the SORS's deadlines in drawing up the GDP data. The two institutions will continue this practice in the future.

The revision of the statistics on international economic relations was two months earlier …

In 2010 the Bank of Slovenia received data on VAT refunds and excise duties of foreign embassies in Slovenia via the SORS, based on which it was able to estimate consumption by foreign embassies. This figure is included in the figure for exports of government services in the balance of payments. Another new data source is the Surveying and Mapping Authority's figures on the values of real estate owned by non-residents, which were obtained in 2010 and included in the figures for the period since 2008.

… and involved new data sources.

Bilateral figures on transfers that certain countries (Bosnia and Herzegovina, Croatia, Serbia, Macedonia and Montenegro) identify in their data systems for payments to/from the rest of the world as remittances from their citizens in Slovenia to the home country were also obtained in 2010. The figures are the source for the item of workers' remittances for the period since 2008.

A survey of household finance assets and consumption was conducted.

In autumn 2010 the Bank of Slovenia conducted the practical part of a new survey of household finance assets and consumption, which is being conducted in a harmonised form by all euro area countries, coordinated by the ECB. In Slovenia the survey data will be supplemented with the available administrative data. The results will be sent to the ECB in 2011 and published on the Bank of Slovenia's website.

The Bank of Slovenia also sends the ECB certain data in the areas of general government and general economic statistics, such as data for the Maastricht economic criteria on long-term interest rates, the state budget position, the general government debt and the HICP, other figures from the national accounts statistics, labour statistics, and data on the excessive deficit procedure. This data is compiled by the SORS and/or the Ministry of Finance in accordance with the aforementioned MoU.

The Bank of Slovenia releases macroeconomic data on Slovenia on its website in accordance with the IMF's Special Statistical Data Dissemination Standards (SDDS). These standards require the regular publication of methodologically sound macroeconomic figures according to an advance release calendar. The Ministry of Finance and the SORS also contribute relevant data for publication in accordance with these standards.

Key financial and macroeconomic data for Slovenia are published in a monthly bulletin and in annual publications on direct investments and financial accounts. All publications, along with information on the extended data series from the bulletin and certain other important data, are also published on the Bank of Slovenia's website. In addition to domestic recipients, the more important direct recipients of the statistical data are the ECB, Eurostat, the IMF and the BIS.

Expert statistical support for the central banks of Albania and Montenegro.

In 2010 the Bank of Slovenia provided expert support to the central banks of Albania and Montenegro in the area of balance of payments statistics in the form of two-day visits to the Financial Statistics Department.

2.1.8 Information system

The Bank of Slovenia is linked to the ESCB's information system.

Article 55 of the Bank of Slovenia Act (Official Gazette of the Republic of Slovenia, No. 72/06) states that, as of the day that the Republic of Slovenia joined the European Union, the Bank of Slovenia shall cooperate with the ECB in accordance with the Statute of the ESCB and of the ECB as regards the recording, collection, processing and disclosure of data and information relevant to the performance of its functions.

Infrastructure of the ESCB's information system.

The Bank of Slovenia is technically linked to the information system of the ECB and ESCB via the ESCB's physical network infrastructure system,[14] the ESCB's application network infrastructure system,[15] the ESCB's system for the secure exchange of e-mail[16] and via a teleconferencing system. Infrastructure equipment is situated at primary and backup locations at the Bank of Slovenia.

14 Core Network.
15 ESCB-Net.
16 ESCB Mail.

The link to the ECB is provided using the ESCB's physical network infrastructure system. It is a high-availability secure private network that links the individual national central banks (NCBs) with the ECB. The ECB is responsible for the system administration of this network, including equipment installed at the NCBs.

The ESCB's application network infrastructure system represents a portion of the infrastructure used to link the NCBs with the ECB. It comprises several multi-purpose servers, firewalls, network switches, etc. All equipment is duplicated to ensure a high level of availability. Some of the equipment is at the Bank of Slovenia's backup computer centre, which allows the link to the ECB to be maintained without disruption in the event of a disaster at the Bank of Slovenia's primary computer centre. All of the equipment of this network that is located at Bank of Slovenia sites falls under its administrative domain.

The aforementioned infrastructure equipment must be upgraded regularly with regard to technological development, increases in the quantity of data and the increased requirement of commercial users. Thus 2010 saw the completion of the project to optimize the ESCB's physical network infrastructure system and application network infrastructure system, while the teleconferencing system was also upgraded. The Bank of Slovenia's backup computer centre was renovated, and moved to a new location.

Applications of the ESCB's information system.

A number of applications, via which data is exchanged between the NCBs and the ECB and ESCB, run on the aforementioned infrastructure. A good deal of activity in the ESCB system in 2010 was devoted to providing application support for the implementation of crisis measures. Thus in 2010 the Bank of Slovenia was also obliged to modify and provide application support, most notably in the theoretical valuation of securities using prices from the valuation hub, in the introduction of debt certificates, in the introduction of non-marketable assets and in the reporting of balance sheet items.

2.2 Other tasks

2.2.1 Banking supervision and ensuring financial stability

Licensing

Licensing credit institutions is one of the Bank of Slovenia's important tasks. In 2010 the Bank of Slovenia issued authorisations to acquire a qualifying holding in a bank, to provide mutually recognised and additional financial services, to merge a legal entity with a bank and to hold office as a member of a bank's management board. The decision to grant or refuse an authorisation is taken by the Governing Board of the Bank of Slovenia based on the opinion of the License Committee, except in the case of authorisations to hold office as a member of a bank's management board, where the decision is based on the opinion of the Commission of the Governing Board of the Bank of Slovenia for the Preparation of Opinions for the Issue of Authorisation to Hold Office as a Member of a Bank's Management Board.

The Bank of Slovenia issued 14 authorisations in 2010, the majority to hold office as a member of a bank's management board.

In 2010 the Bank of Slovenia issued a total of 14 authorisations, and rejected one request for the issue of authorisation to hold office as a member of a bank's management board. The majority of authorisations (eight) issued in 2010 were to hold office as a member of a bank's management board. Three authorisations were issued to provide additional financial services and one to provide mutually recognised financial services. The Bank of Slovenia also issued one authorisation in 2010 to acquire a qualifying holding in a bank and one to merge a legal entity with a bank. Fewer authorisations were issued in 2010 than in 2009, when 22 were issued, 15 of which were authorisations to hold office as a member of a bank's management board.

In 2010 the Bank of Slovenia received 22 notifications of the direct provision of services and one notification to expand the activities of a branch.

Pursuant to Directive 2006/48/EC (previously: Directive 2000/12/EC) and Annex I (List of activities subject to mutual recognition), a bank of a Member State that is entitled to provide banking services and other (mutually recognised) financial services may also provide these services in Slovenia. It may provide them via a branch *(in the case of permanent pursuit of business)* or directly *(in the case of occasional provision of services without elements of permanent presence in Slovenia)* without an authorisation from the Bank of Slovenia, which must be notified in writing by the relevant supervisory authority in the home Member State. In 2010 the Bank of Slovenia received 22 notifications of the direct provision of banking or other mutually recognised financial services (compared to 28 notifications the previous year) and one notification of the expansion of mutually recognised financial services via an already functioning branch. A list of banks of EU Member States that have carried out the notification procedure for the provision of banking services and other financial services in Slovenia via their home banking supervisors is available on the Bank of Slovenia’s website. Different arrangements apply to the banks of third countries. Banks of third countries may only provide banking and other (mutually recognised) financial services via a branch, Bank of Slovenia authorisation being required to establish the branch. The Bank of Slovenia may request that the bank of a third country deposit a specific sum of cash or other eligible collateral in Slovenia, or provide other appropriate collateral as a guarantee for the settlement of liabilities from transactions concluded in Slovenia.

Examinations of banks and savings banks

In line with the development of macroeconomic conditions, the greatest emphasis during examinations was on credit, liquidity and operational risks.

In 2010 the Banking Supervision Department conducted regular on-site examinations of banks and savings banks, which are based on assessing the level of risks and the quality of the risk management control environment. Examinations of specific areas of risk were prevalent among the examinations conducted at banks and savings banks, practice having shown that shorter and thus more frequent and more detailed examinations of specific areas are more significant and more needed than comprehensive examinations (full-scope examinations). The greatest emphasis was placed on credit, liquidity and operational risks (in the scope of capital and strategic risk), in line with the development of macroeconomic conditions. Special attention was given to the ongoing monitoring of the implementation of measures and to follow-up examinations of the implemented measures.

The Banking Supervision Department also carried out specific examinations regarding compliance with legislation in the area of money laundering and terrorist financing, the ability of banks to provide data regarding guaranteed deposits and the readiness of banks to use loans as collateral for Eurosystem claims, and regarding other, more specific areas of banking operations.

The monitoring of the effects of the implementation of Basel II rules with respect to the calculation of capital requirements and capital adequacy continued in 2010.

In 2010 the Banking Supervision Department continued to systematically monitor the effects of the implementation of the new European capital framework at banks and savings banks with respect to the calculation of capital requirements in accordance with the rules of Basel II. Focus was placed on the quantitative portion of the internal capital adequacy assessment process, a detailed examination of the entire process and the calculation of capital requirements having been carried out at certain banks. To that end, examinations were also carried out of the readiness of individual banks for the introduction of the advanced approaches for calculating capital requirements for credit (IRB)[17] and operational (AMA)[18] risk, and for controlling the proper functioning of these approaches and selected models at individual banks.

Intensive cooperation with foreign supervisors on the basis of multilateral agreements on the functioning of supervisory colleges is ongoing at the banks under majority foreign ownership. All supervisors responsible for the supervision of an entire banking group participated in these colleges, the primary aim of which is to achieve more comprehensive and better coordinated supervision of banking groups that operate internationally. The Bank of Slovenia participates in six supervisory colleges. The supervisory colleges discuss and coordinate examinations of the implementation and use of advanced approaches for calculating capital requirements. The procedure that results in a joint decision regarding the initial use of an advanced approach is led by the supervisor of a banking group's parent bank. In such cases the Bank of Slovenia participates as a host supervisor, responsible for a subordinate bank.

The Bank of Slovenia is responsible for the organisation and management of the supervisory college for a Slovenian banking group. The last meeting of the college was held in October 2010 and attended by all supervisors of the countries where the bank has subsidiaries.

The Banking Supervision Department also maintains regular bilateral links with all supervisors with whom memoranda of understanding have been signed (the Bank of Slovenia has a total of 12 memoranda of understanding with foreign supervisory institutions). To that end, Bank of Slovenia supervisors participated in two examinations of the operations of subsidiary banks.

Based on authorisations from the Governor of the Bank of Slovenia, 39 examinations were initiated in 2010. The Banking Supervision Department carried out the following activities in the scope of examinations initiated in previous years:

Supervisors carried out 84 examinations at banks in 2010. The majority of measures imposed during supervision related to credit risk.

- 35 on-site examinations by individual area of risk and the control environment,
- 32 follow-up examinations to verify implemented measures,
- 17 broader thematic examinations,
- participation in two examinations of banks and other financial institutions abroad, that are owned by Slovenian banks, and
- several examinations of the implementation of measures and several one-day examinations of a specific area of a bank's operations.

Based on the examinations at banks and savings banks, the Bank of Slovenia may issue recommendations, warnings or orders, in accordance with the Banking Act. By the end of 2010 the Bank of Slovenia had issued 9 orders to rectify breaches with 26 points, 95 warnings and several requests for reporting and the fulfilment of conditions for the issue of authorisations, and recommendations for improving operations. The majority of measures issued related to credit risk, followed by

17 Internal Ratings-Based Approach (IRB)
18 Advanced Measurement Approach (AMA)

liquidity and operational risk, and the organisational structure and governance of banks. All of the aforementioned measures were discussed and approved by the Governing Board of the Bank of Slovenia.

In 2010 the Bank of Slovenia approved three requests for the granting of authorisation to include subordinated debt in Tier 1 additional own funds.

In line with the Core Principles for Effective Banking Supervision, the Banking Supervision Department of the Bank of Slovenia maintains regular contact with the management of banks and savings banks through channels including regular annual meetings held at the completion of an examination and otherwise. The primary purpose of these meetings is to assess the performance and position of a particular bank or savings bank and to become familiar with its strategy for future development. The exchange of opinions and information between supervisors and the management of banks or savings banks is also a prerequisite for timely and appropriate action in the event of operating difficulties. The Banking Supervision Department continued this practice in 2010, and conducted a number of interviews with the management of banks and savings banks.

Cooperation between supervisory authorities includes the exchange of information and findings obtained during the supervision of financial institutions.

Because of a joint concern and responsibility for the stability of the entire financial system and interdependence of financial institutions, cooperation between competent sectoral supervisory authorities (the Bank of Slovenia, the Securities Market Agency and the Insurance Supervision Agency) was of high importance also in 2010. Cooperation was carried out on routine basis set by the rules on mutual cooperation between supervisory authorities. It included regular meetings, the exchange of information and the conducting of joint examinations. Supervisory authorities are required to inform each other if they identify any irregularities relating to the work of other institutions.

Changes to banking regulations

Two amendments to the Banking Act were adopted owing to changes in several EU directives. A significant portion of secondary legislation was thus amended in the form of regulations.

The majority of changes to secondary legislation in 2010 were the result of amendments to the Banking Act (Official Gazette of the Republic of Slovenia, No. 98/09; hereinafter: the ZBan-1D and Official Gazette of the Republic of Slovenia, No. 79/10; hereinafter: the ZBan-1E) and the new Consumer Credit Act (Official Gazette of the Republic of Slovenia, No. 59/10; hereinafter: the ZPotK-1).

A new *Regulation on the deposit guarantee scheme*, linked to changes in the area of deposit guarantees as the result of the new ZBan-1D, was issued at the beginning of the year. Amendments to the regulation derive from an increase in the guaranteed deposit amount from EUR 22,000 to EUR 50,000[19], a new definition of net deposit, changes regarding deposits excluded from the guarantee scheme and the treatment of deposits on custodian accounts. Content that was previously included in the text of the related act was also excluded. Therefore, the *Guidelines for completing and submitting guaranteed deposit reports* were also reissued.

The *Regulation on the amounts of annual fees for supervision and fees for decisions regarding requests for the granting of authorisation was* also amended in January.

[19] The guaranteed deposit amount was increased to EUR 100,000 from 31 December 2010 onwards by the amendment to the ZBan-E1 (Official Gazette of the Republic of Slovenia, No. 79/10 of 8 October 2010).

The ZBan-1D redefined the obligation to pay fees to include the granting of authorisations issued ex officio by the Bank of Slovenia. These include authorisations relating to the calculation of capital requirements according to advanced approaches issued by the Bank of Slovenia to the banks and subordinated banks of other member states, if the supervisory authorities of these countries are responsible for supervision on a consolidated basis.

The new *Regulation on electronic money issuing companies* was issued in February owing to the new definition of the term electronic money, as used in the ZBan-1D and deriving from the Payment Services and Systems Act (Official Gazette of the Republic of Slovenia, No. 58/09). Electronic money is no longer treated as a payment instrument, but as money or a monetary value saved in electronic format, and used as legal tender for primarily small value payments.

Amended in March was the *Regulation on the calculation of capital requirements for credit risk using an internal ratings-based approach*, whereby banks intending to use the IRB approach were, in line with practices in other EU Member States, provided the opportunity to extend the envisaged five-year period for the gradual introduction of the IRB approach. Every extension of the five-year period must be justified and documented.

Regulations laying down conditions for credit assessment institutions have become more stringent owing to the crisis.

The *Regulation on the recognition of external credit assessment institutions* was amended in August owing to Regulation (EC) No. 1060/2009 of the European Parliament and of the Council of 16 September 2009 on credit rating agencies (hereinafter: the EC Regulation), which also covers the use of credit rating for the regulatory purposes of credit institutions and other regulated financial corporations. Since the end of 2010, external credit rating institutions registered in accordance with the EC Regulation are considered to have complied in full with all four standards relating to the assessment methodology. The EC Regulation also took into account changes from the Revised Guidelines on the recognition of external credit assessment institutions.

Two secondary regulations, based on or related to the requirements of the ZPotK-1, were adopted by the Bank of Slovenia in September: *the Regulation on the conditions to be met by credit intermediaries and the Regulation on reporting the effective interest rates of banks and savings banks in accordance with the Consumer Credit Act*. While the changes to the second regulation were only editorial in nature, the first regulation brought changes arising from amended legislation and changes linked to findings from practice. This required changing the definition of certain terms (e.g. credit intermediary), additional requirements regarding the disclosures of a credit intermediary's authorisations with respect to advertising and documents intended for consumers, and with regard to contracts that form the basis for the provision of credit intermediary services by a credit intermediary. The requirements for reporting data to the Bank of Slovenia regarding credit intermediaries and transactions with them were supplemented. In accordance with the new regulation, banks must also publish on their websites lists of the credit intermediaries with whom they transact and update this data regularly.

Amendments were also published to the *Guidelines for implementing the regulation on the assessment of credit risk losses of banks and savings banks*, the most important part of which relates to additional clarification regarding the data in column 22 of the RAZ-1 form, which relates to unsecured financial assets and commitments and contingent liabilities, and to the inclusion of derivatives in column 6 of the aforementioned form.

Amendments to three directives resulted in changes to a number of regulations that entered into force at the end of 2010.

Three directives were adopted in 2009 that amended the banking directive (2006/48/EC) and the directive on the calculation of capital requirements for market risks (2006/49/EC): Directive 2009/111/EC (the so-called CRD II directive), 2009/83/EC and 2009/27/EC. Twelve Bank of Slovenia regulations required amending owing to the transposition of the aforementioned regulations and the introduction of guidelines by the Committee of European Banking Supervisors. Given that the CRD II brought about more significant changes with regard to the treatment of own fund instruments, large exposures and securitisation, the most significant changes were likewise made to the regulations that govern the aforementioned areas: *the Regulation on the calculation of the capital of banks and savings banks, the Regulation on large exposures of banks and savings banks, the Regulation on the calculation of capital requirements for credit risk in securitisation and the Rules regarding the exposure of banks and savings banks to credit risk transfer.* The CRD II directive results in more significant changes to liquidity risk management, which is governed by the *Regulation on risk management and implementation of the internal capital adequacy assessment process.* Appendix V to the aforementioned regulation was therefore completely revised. Changes to other regulations[20] were primarily of a technical or editorial nature. In accordance with the deadlines for the transposition and entry into force of the new rules set out in the above stated EC directives, all of the aforementioned regulations were published in October and entered into force on 31 December 2010.

The guarantee on deposits was standardised; all deposits up to EUR 100,000 are guaranteed since the end of 2010.

The new ZBan-1E, published in October 2010, once again brought changes to the deposit guarantee scheme linked to the transposition of the provisions of the new guarantee directive into Slovenian law. One of the purposes of legislative changes was to ensure the conditions for the payment of guaranteed deposits in the shortest possible deadlines. A more detailed definition of the latter was one of the more significant changes to the new *Regulation on the deposit guarantee scheme*, issued in December on the basis of the ZBan-1E. In addition to the aforementioned change, the regulation also resulted in a decrease in the proportion used to calculate banks' liabilities from investments in the prescribed financial instruments aimed at ensuring liquid funds in the event of the payment of guaranteed deposits.

The ZBan-1E also brought changes to certain other areas that required relevant changes to secondary legislation issued by the Bank of Slovenia. Changes were made to the *Regulation on the amounts of annual fees for supervision and fees for decisions regarding requests for the granting of authorisation* owing to the amended basis for calculating annual fees for supervision, and amended or new authorisations related to the calculation of capital and the maximum permitted exposure of banks. Three regulations required amending due to the shortening of the deadline for the submission of unaudited annual financial statements: *the Regulation on books of account and annual reports of banks and savings banks, the Regulation on the supervision of banks and savings banks on a consolidated basis and the Regulation on the investments of banks and savings banks in qualifying holdings in entities in the non-financial sector.* All of the aforementioned regulations were issued in December 2010.

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20 The Regulation on the calculation of capital requirements for credit risk using the standardised approach for banks and savings banks, the Regulation on the calculation of capital requirements for credit risk using an internal ratings-based approach for banks and savings banks, the Regulation on credit protection, the Regulation on the calculation of capital requirements for market risks for banks and savings banks, the Regulation on the calculation of capital requirements for operational risk for banks and savings banks, the Regulation on disclosures by banks and savings banks, the Regulation on the reporting of capital and capital requirements of banks and savings banks and the Regulation on the reporting of individual facts and circumstances of banks and savings banks.

Financial stability

In accordance with legally prescribed objectives, the Bank of Slovenia analysed the financial stability of the Slovenian financial system in 2010. In spring it published the *Financial Stability Review*, in which it comprehensively analyses the Slovenian financial system annually in terms of risk exposure. The analysis *Macro Stress Tests for the Slovenian Banking System*, with the simulation of possible shocks, was completed in early autumn. The drafting and publication of the analysis *Stability of the Slovenian Banking System* followed at the end of the year.

Lending to non-financial corporations has stagnated, while the quality of the baking system's credit portfolio has deteriorated.

The *Financial Stability Review* analysed economic developments in 2009 and early 2010 in terms of systemic risks. It was determined that certain risks rose during this period. The sensitivity of the financial system to potential shocks was therefore relatively high. Characteristic of the reporting period was the gradual recovery of the Slovenian economy, which has been reflected in low and unstable quarter-on-quarter GDP growth since the second quarter of 2009. The extent of the consequences of the economic crisis on the Slovenian financial system and economy is still being determined. This has been seen at banks as a stagnation in corporate lending and as a deterioration in the quality of their credit portfolio. In addition to tightened financing via bank loans, companies have also felt the decline in economic activity as a decrease in commercial financing, which has further increased their financial needs, and resulted in a deterioration in liquidity and increased payment indiscipline.

Slovenia is highly sensitive to changing financing conditions on the international financial markets.

The restructuring of the sources of Slovenian banks' funding had yet to be completed in 2009. Banks have primarily obtained short-term funding, which is not a stable basis for the beginning of a new credit cycle. The decline in liabilities to foreign banks during the reporting period was largely offset by liabilities to the Eurosystem and by government deposits. The Slovenian economy's dependence on foreign sources of financing has not diminished, as the government has raised funds through bond issues in the rest of the world. Slovenia's considerable sensitivity to changing financing conditions on the international financial markets has therefore remained unchanged, particularly in the context of the rising debt problems faced by certain euro area countries.

Alongside refinancing risk, credit risk has become the most significant risk for banks.

The *Financial Stability Review* warned that credit risk has become the most significant risk for banks. The quality of the credit portfolio deteriorated during the reporting period, which had an adverse impact on banks' operating results in the form of rising impairment and provisioning costs. It was determined that a likely rise in market interest rates and a decrease in the volume of relatively less expensive sources of funding will result in a rise in bank funding costs. In the Financial Stability Review, the Bank of Slovenia warned of increasing income risk at banks and of the importance of still-low interest-rate risk. The review finds that maintaining capital adequacy has become more important than growth in lending, and warns that timely increases in banks' capital are necessary for financial stability, and with it the acceptance of responsibility for repairing past decisions concerning the take-up of credit risk.

The report *Macro Stress Tests for the Slovenian Banking System* forecasts the banking system's balance sheet over the next two-year period. Using an integrated approach, the banking system's sensitivity to the simulated shocks of rising interest rates, declining GDP growth and the suspension of financing on wholesale markets is assessed. Credit risk with respect to individual shocks was assessed using a piecewise approach with a credit risk model.

The analysis *Stability of the Slovenian Banking System* illustrates developments over the first three quarters of 2010. In this analysis, the Bank of Slovenia finds that the development of financial risks in the Slovenian banking system during this period was under the influence of the continuing gradual and unstable domestic economic recovery and the uncertain situation on the European financial markets. Investment as a proportion of GDP has remained at the level of the national savings rate, or down one third on 2007 and 2008. Slovenia's financial liabilities to the rest of the world were up owing to the issue of securities, which increased Slovenia's dependence on foreign sources of financing. Refinancing risk has remained pronounced primarily at the banks under majority domestic ownership.

The analysis *Stability of the Slovenian Banking System* warns of rising credit risk.

The analysis warned of rising credit risk. The proportion of non-performing claims rose during the reporting period, while clients' arrears in the settlement of liabilities to banks have lengthened. The Bank of Slovenia warned of the continuing increase in non-performing claims and impairment costs, and of the expected adverse impact these will have on the banking system's profitability and capital. It was determined that banks are attempting to redistribute a portion of their credit exposure from the construction sector to households by increasing housing loans. In its report, the Bank of Slovenia warned that income risk will be of increasing importance to banks in the future owing to rising impairment and provisioning costs, low growth in lending and funding costs.

Key risks will continue to rise at banks in the future.

The banking system's solvency during the reporting period was relatively low with respect to the average of comparable EU banks. The surplus of regulatory capital over capital requirements, which reflects the banking system's capacity to absorb risks, exceeded 30%. In its analysis, the Bank of Slovenia warns that the banking system requires decisions by bank owners regarding changes to the manner of operations that will halt the adverse trends as soon as possible. It gave as possible measures stricter collection procedures and the exclusion of bad claims from banks' balance sheets, an increase in loans to good clients with the appropriate collateral, capital increases and consolidation. The report's expectations for the near future included a contraction in the banking system's balance sheet, an increase in key risks and operating losses by certain banks.

2.2.2 Payment services for Bank of Slovenia clients

Administration of budget user accounts

The Bank of Slovenia administers the treasury account of the government and municipalities.

The Bank of Slovenia administers the government’s single treasury account and 204 standard municipal treasury accounts, open in a number of currencies. The accounts of direct and indirect users of the national and municipal budgets, the Health Insurance Institute and the Pension and Disability Insurance Institute (included in the single treasury account system as set out in the Public Finances Act), were opened as sub-accounts of the government or municipal treasury accounts. The sub-accounts are managed by the Public Payments Administration, to which direct and indirect users of the national and municipal budgets present payment orders and from which they receive the full set of return information about payments transacted.

In 2010 EUR 41.186 billion in inflows and EUR 41.186 billion in outflows were processed through the government’s single treasury account, and EUR 36.587 billion in inflows and EUR 36.589 billion in outflows through municipal treasury accounts.

In addition to the single treasury accounts, the Bank of Slovenia also manages 35 special purpose accounts for the government and other budget users.

Administration of accounts for the KDD and KDD members

The Bank of Slovenia administers a guarantee fund cash account and a fiduciary account for the custodian services of the Central Securities Clearing Corporation (KDD). In addition, the Bank of Slovenia also administers the accounts of KDD members, via which cash settlements are made for securities transactions. At the end of 2010 there were 22 KDD members, including 14 commercial banks and 8 investment firms, with open transaction accounts for customer funds and clearing accounts at the Bank of Slovenia.

The Bank of Slovenia administers a guarantee fund cash account and a fiduciary account for the custodian services of the CSCC.

In 2010, EUR 2.924 billion in inflows and EUR 2.924 billion in outflows were processed through the KDD accounts and KDD member accounts.

Administration of accounts for foreign financial institutions and EU institutions

The Bank of Slovenia also administers the accounts for foreign financial institutions and EU institutions, via which inflows of EUR 795.7 million and outflows of EUR 778.5 million were processed in 2010.

The Bank of Slovenia administer an account for the European Commission.

2.2.3 Management of the Bank of Slovenia's financial investments

The Bank of Slovenia's financial investments include all of its financial assets not related to the implementation of monetary policy. They comprise financial investments denominated in domestic and foreign currencies. The value of the Bank of Slovenia's financial investments as at 31 December 2010 was EUR 5,045.7 million, of which EUR 4,242.5 million was investments in financial instruments, which are either claims against euro area residents or claims against non-euro residents denominated in euro. These include EUR 3,924.7 million of investments in capital market instruments, EUR 15.0 million in money market instruments and EUR 302.8 million in cash and deposits. In addition, EUR 803.2 million was invested in financial instruments, which are claims against non-euro area residents denominated in non-euro currencies and meet the criteria of international monetary reserves. The volume of financial investments is also dependent on the level of liabilities to the Eurosystem.

The value of the Bank of Slovenia's financial investments as at 31 December 2010 was EUR 5,047.7 million.

Table 4: **Balance of the Bank of Slovenia's financial investments**

In EUR million	Financial investments of the Bank of Slovenia		
Balance as of:	Investments in euros and all investments in instruments of euro area issuers	International monetary reserves	Total
31. Dec 2007	4,820.0	727.9	5,547.9
31. Dec 2008	4,667.7	687.2	5,354.9
31. Dec 2009	4,118.7	749.1	4,867.7
31. Dec 2010	4,242.5	803.2	5,045.7

Source: Bank of Slovenia

According to the International Monetary Fund's definition, cash in foreign currency and foreign exchange holdings abroad, gilt-edged securities, monetary gold, holdings of SDRs and the reserve tranche at the International Monetary Fund are considered international monetary reserves. Since 1 January 2007 Slovenia has applied the definition applied by all other euro area Member States in the statistical treatment of international monetary reserves. In addition to monetary gold, the reserve tranche and SDRs, that portion of foreign currency reserves not denominated in euro and placed outside the euro area is contributed to international monetary reserves. The methodology is explained in detail in the article, *Statistical Treatment of International Monetary Reserves Following Slovenia's Entry to the Euro Area* (Surveys and Analyses, May 2007).

A three-level decision making process is employed in the management of financial assets.

The management of the Bank of Slovenia's financial investments is based on a three-level decision-making process. The Governing Board of the Bank of Slovenia sets out the *Guidelines for Managing the Bank of Slovenia's Financial Investments*, which define the long-term policy for the management of the Bank of Slovenia's financial investments and defines management objectives. The second level in the process is represented by the *Investment Committee*, which prescribes the *Criteria for Managing the Bank of Slovenia's Financial Investments* in order to limit exposure to various types of risk. The Investment Committee also defines the methodology for measuring performance and for quantifying risks. At the third level, portfolio managers carry out the operational aspect, within set tolerances.

The current credit risk management criteria allow investments in financial instruments exposed to sovereign and banking types of risk, issued by issuers with an internal rating of at least A-. The ratio of the size of investments exposed to sovereign and banking risk is also prescribed. Investments in the state and banking sector are limited to a list of eligible issuers, whereby there is also an upper limit on exposure to an individual entity to sovereign risk or to an individual banking group. The upper exposure limit depends on the Bank of Slovenia's internal rating.

Investment policy is defined in management criteria.

The currency exposure of the Bank of Slovenia's investments and the limits on permitted deviations are precisely set out in the criterion for managing currency risk. The criterion also lays down a target currency structure for investments. In 2007 an additional instrument, i.e. a foreign exchange swap instrument was added to the list of eligible instruments, which allows for exposure to individual types of currency risk, while hedging against changes in the exchange rate itself. In this manner, the Bank of Slovenia hedged the entire foreign currency exposure in January 2008, with the exception of the portion of investments representing the amount potentially called into international monetary reserves by the ECB. The criterion for managing interest-rate risk specifies the modified duration of financial investments, and lays down the maximum allowable deviation from the target modified duration. The criterion for managing liquidity risk specifies a minimum amount of liquid assets. The criteria for managing the Bank of Slovenia's financial investments also set out the terms for securities lending and other activities. The Bank of Slovenia's investment policy must comply with Article 123 of the Treaty on the functioning of the European Union[21], which prohibits the monetary financing of public sector institutions. The prohibited forms of public institution financing include investment deposits and purchases of primary issued securities, commercial paper and certificates of deposit if the issuer is public sector. Purchasing EU public sector financial instruments on the primary market is prohibited, while investments are permitted on the secondary market within a fixed limit for each country. The management of the Bank of Slovenia's financial investments was carried out in line with the aforementioned criteria during 2010. More detailed information on the

[21] Article 123 of the Treaty on the functioning of the European Union replaced Article 101 of the Treaty establishing the European Community.

structure of the international monetary reserves as at 31 December 2010 is given in the section on the financial statements.

2.2.4 International cooperation

European Union

In 2010 the Governor of the Bank of Slovenia participated in informal sessions of ECOFIN (meetings of financial ministers, with the governors of EU Member State central banks in attendance).

In 2010 Bank of Slovenia experts also attended sessions of committees, working groups and other bodies that are active within the institutions of the EU with a focus on financial and monetary matters. These include sessions of the Economic and Financial Committee (EFC) and its subcommittees, meetings of the Committee of European Banking Supervisors (CEBS) and its working groups, meetings of the Committee on Monetary, Financial and Balance of Payments statistics (CMFB) and other working groups from the relevant area that are active within the European Commission and the EU Council.

The European Systemic Risk Board was established in December 2010.

The European Systemic Risk Board (ESRB) is a new European body established on 16 December 2010 in the scope of reform of the EU financial sector supervision system. It is responsible for the macro-prudential supervision of the financial system of the European Union as a whole, and for monitoring and assessing risks to the stability thereof. The Governor of the Bank of Slovenia is a member of the General Board, which takes the decisions necessary to ensure the performance of the tasks entrusted to the ESRB. The ESRB is chaired by the President of the ECB.

IMF

In accordance with Slovenian law, the Bank of Slovenia is responsible for the Republic of Slovenia's cooperation within the IMF, while the Governor of the Bank of Slovenia is a member of the IMF Board of Governors.

The Act amending the Act on Membership of the Republic of Slovenia in the IMF was adopted in April 2010.

In order to ensure the additional IMF funds required by the global financial turmoil and economic crisis, the level of Slovenia's participation in the IMF's financial arrangements was also enhanced. The Act amending the Act on Membership of the Republic of Slovenia in the International Monetary Fund was therefore adopted in April 2010. The amended act consistently segregates the extent and content of the obligations of the Bank of Slovenia and Republic of Slovenia to the IMF.

Slovenia's quota at the IMF was unchanged at SDR 231.7 million, representing 0.12% of the voting power of all IMF members. In accordance with Resolution 63-2 on the Reform of Quota and Voice in the IMF, which the Board of Governors approved in April 2008, the quotas and voting shares of the 54 members were to have increased, including the quota and voting share of Slovenia. The aforementioned increase in quotas did not occur in 2010, as the adopted resolution calls for an amendment of the Articles of Agreement of the IMF, which requires approval by at least three-fifths of the membership, with 85% of the total voting power.

In December 2010 the Board of Governors approved the reform of quotas and governance of the IMF, which also included the 14th general review of quotas. The reforms, which entail the doubling of Slovenia's quota, are expected to take effect by the Annual meetings of the IMF and World Bank in 2012.

Since 1998 Slovenia has contributed to financing IMF loans under the Financial Transaction Plan (FTP). In the second half of 2010 Slovenia contributed funds amounting to SDR 9.0 million under the FTP for lending. At the end of December 2010 Slovenia's reserve tranche position at the IMF stood at SDR 51.1 million, an increase on 2009.

A bilateral borrowing agreement between the Bank of Slovenia and the IMF was signed in September 2010.

A bilateral borrowing agreement between the Bank of Slovenia and the IMF, signed in September 2010, entered into force in October 2010. The majority of European countries signed such agreements back in 2009 owing to the need to increase IMF funding. The amount of Slovenia's bilateral loan is EUR 280 million. The drawing period is not expected to exceed four years.

Representatives of the IMF did not hold regular annual consultations with Slovenia in 2010 pursuant to Article IV of the IMF Statute, as agreement was reached in 2009 with the IMF that Slovenia will be examined in accordance with Article IV of the Statute every two years in the future. Therefore, only a brief staff visit was made to Slovenia in June 2010.

Bank for International Settlements

The Governor of the Bank of Slovenia participated in meetings of central bank governors of BIS Member States, which are organised every two months. Discussions are held on global economic developments and on developments on the international financial markets. The meetings of governors also represent an opportunity to exchange opinions regarding various central bank matters, which in 2010 related primarily to the new framework for supervision of the financial markets. The Bank of Slovenia is a shareholder in the BIS, and its representatives participated in the annual General Meeting of the BIS in Basel.

Organisation for Economic Cooperation and Development

Slovenia became a member of the OECD in July 2010.

Slovenia joined the Organisation for Economic Cooperation and Development (OECD) in July 2010. Slovenia began the process of joining the OECD at the end of 2007, when the OECD Council approved the *Accession Programme for Slovenia's Entry to the OECD*. Negotiations to that end continued until April 2010, and entailed the continued active participation in 2010 of a Bank of Slovenia representative as a member of the interdepartmental working group, the participation of Bank of Slovenia representatives in the drafting of initial positions and participation in discussions before the Committee on Financial Markets, the Investment Committee, the Committee on Statistics and the Steering Group for Corporate Governance. After Slovenia became a member of the OECD, in 2010 Bank of Slovenia representatives also participated in the regular meetings of the Economic Policy Committee, the Committee on Financial Markets and the Working Group on International Investments Statistics.

Technical assistance

The Bank of Slovenia cooperates with other central banks as part of central bank technical assistance. In 2010 the Bank of Slovenia received technical assistance relating to the use of SAP software for financial planning and banking supervision. The Swiss National Bank and the French Autorité de contrôle prudentiel (ACP) offered the Bank of Slovenia technical assistance.

In 2010 the Bank of Slovenia provided technical assistance to the central banks of four countries in south-eastern Europe: Serbia, Montenegro, Kosovo and Albania. Study visits were carried out in the areas of monetary policy, legal issues, statistics, information technology, banking supervision, accounting, organisational protocol and internal auditing. The Bank of Slovenia also facilitated four one-month internships in 2010 for representatives from the aforementioned countries.

In 2010 the Bank of Slovenia participated in the Eurosystem's technical assistance programmes, including the Eurosystem technical assistance programme for the central bank of Bosnia and Herzegovina and the Eurosystem's regional programme „Strengthening Macro and Micro Prudential Supervision in EU Candidates and Potential Candidates".

3 ORGANISATIONAL STRUCTURE OF THE BANK OF SLOVENIA

Governing Board of the Bank of Slovenia

The decision making bodies of the Bank of Slovenia are the Governor of the Bank of Slovenia and the Governing Board of the Bank of Slovenia.

The Governing Board of the Bank of Slovenia comprises five members: the Governor and four Vice-Governors. The Governor may authorise one of the Vice-Governors to be his deputy. The composition of the Governing Board of the Bank of Slovenia as at 31 December 2010 was as follows:

- Marko Kranjec, Ph.D., Governor,
- Darko Bohnec, Vice-Governor,
- Janez Fabijan, MSc, Vice-Governor, and
- Stanislava Zadravec Caprirolo, MSc, Vice-Governor.

The following changes occurred in the composition of the Governing Board of the Bank of Slovenia in 2010:

- At its session of 26 March 2010 the National Assembly adopted a decision on the appointment of Stanislava Zadravec Caprirolo as Vice-Governor and member of the Governing Board of the Bank of Slovenia for a term of six years, beginning on 6 April 2010.
- The employment of Andrej Rant, Deputy Governor, ended on 8 September 2010. The call for the nomination of candidates for a member of the Governing Board of the Bank of Slovenia was published in the Official Gazette of the Republic of Slovenia No. 82/2010 of 18 October 2010.

Organisational structure of the Bank of Slovenia

All of the Bank of Slovenia's work is carried out by employees in the following types of organisational units: sectors, departments, sections and offices (see the organisational chart).

Work between sectors is coordinated in the scope of an individual sector. Sectors are typically coordinated by the Governor, Vice-Governors and a director-coordinator.

Work of an operational nature and other work of a similar nature are carried out at the departmental level. There are 14 departments at the Bank of Slovenia that can be further broken down into sections and offices.

Commissions, committees and working bodies of the Bank of Slovenia

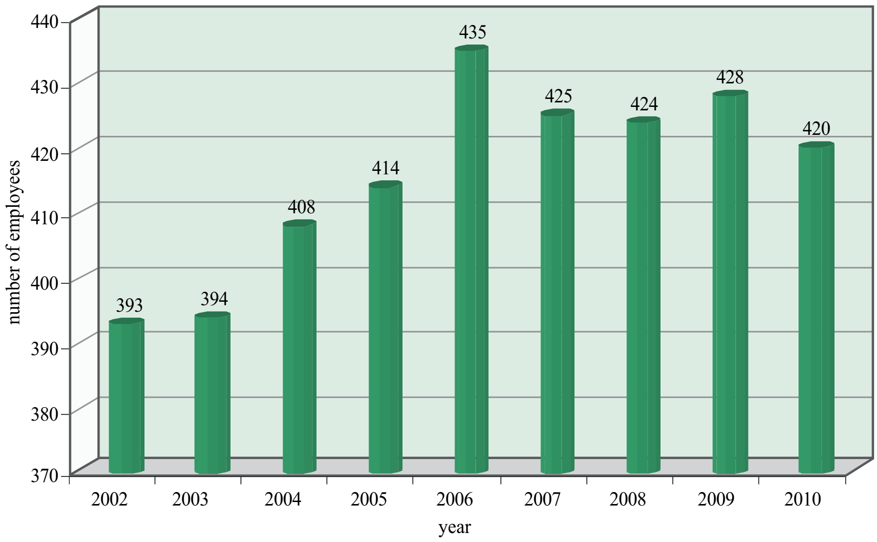
A total of 20 commissions, 5 committees and 6 working groups, covering various areas of operations, function within the Bank of Slovenia. The most important working bodies are as follows:

- License Commission (president: Stanislava Zadravec Caprirolo, since 10 May 2010),
- Commission of the Governing Board of the Bank of Slovenia for the Preparation of Opinions for the Issue of Authorisations to Hold Office as a Member of a Bank's Management Board (president: Darko Bohnec, since 10 May 2010),
- Research Commission (president: Tomaž Košak, MSc),
- Audit Committee (president: Dušan Zbašnik, Ph.D.),
- Investment Committee (president: Ernest Ermenc since 7 September 2010),
- Operational Risk Committee (president: Darko Bohnec),
- Liquidity Commission (president: Tomaž Košak, MSc),
- Violations Commission (president: Jasna Iskra since 2 March 2010), and
- Crisis Management Group (president: Stanislava Zadravec Caprirolo, since 1 December 2010).

Employees

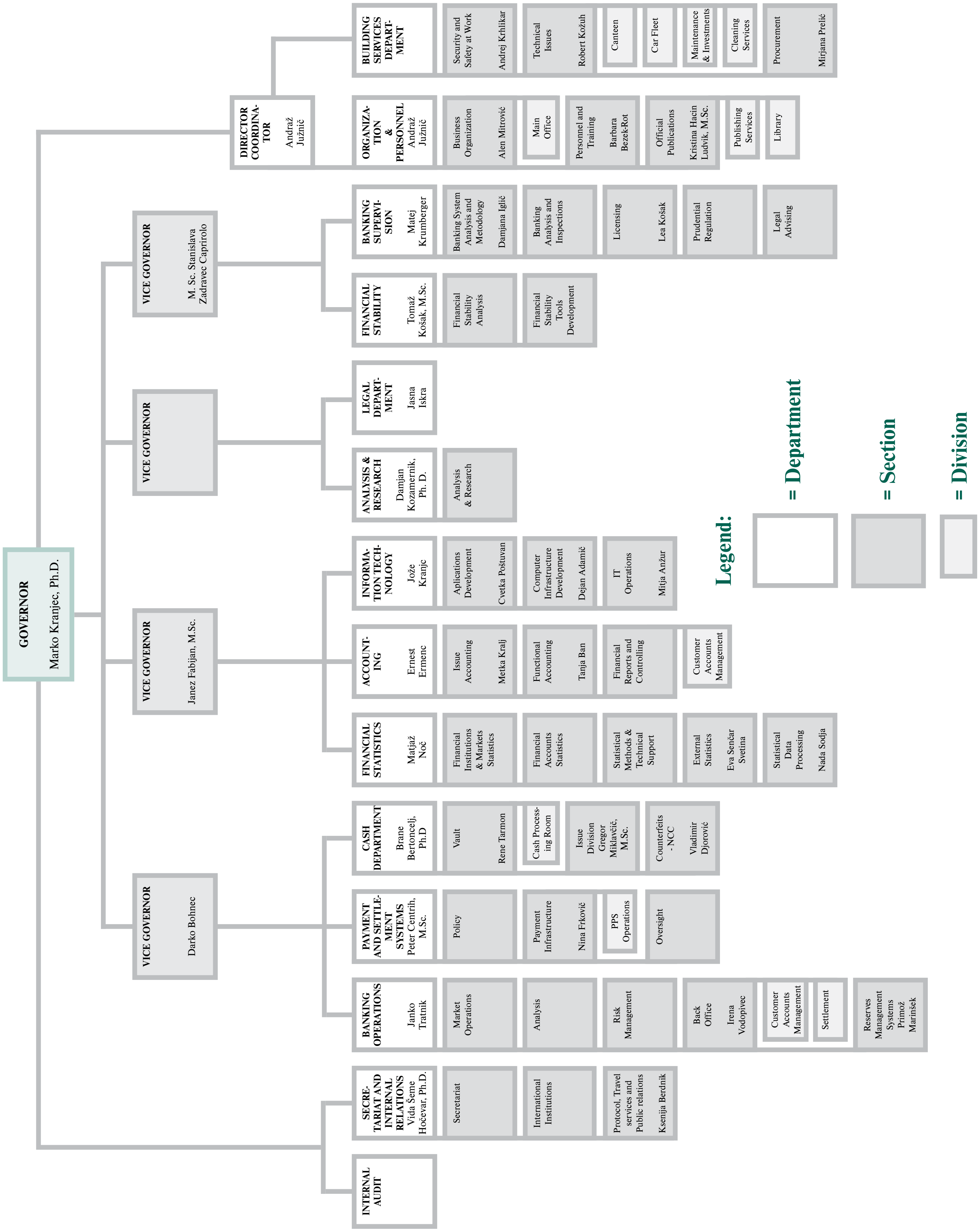
The Bank of Slovenia had 420 employees as at 31 December 2010.

Figure 30: **Number of employees at the Bank of Slovenia as at the final day of the year**



Source: Bank of Slovenia

Organisational structure of the Bank of Slovenia as at 31 December 2010



4 FINANCIAL STATEMENTS

Financial statements of the Bank of Slovenia for the Year 2010

Statement of responsibilities of the Governing Board

The Law on the Bank of Slovenia (the Bank) and the Statutes of the Bank require the Governing Board to prepare financial statements for each financial year which give a true and fair view of the state of affairs of the Bank and the surplus or deficit of the Bank for that period. In preparing those financial statements the Governing Board is required to:

- Select suitable accounting policies and then apply them consistently;
- Make judgements and estimates that are reasonable and prudent;
- State whether applicable accounting standards have been followed; and
- Prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Bank will continue in business.

The Governing Board has a general responsibility for taking such steps as are reasonably open to it to safeguard the assets of the Bank.

Deloitte.

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INDEPENDENT AUDITOR'S REPORT

To the Governing Board of the Bank of Slovenia

Report on the Financial Statements

We have audited the accompanying financial statements of Bank of Slovenia (the 'Bank'), which comprise the balance sheet as at December 31, 2010 and the income statement for the year then ended and a summary of significant accounting policies and other explanatory notes.

Responsibility for the Financial Statements
The Governing Board is responsible for the preparation and fair presentation of these financial statements in accordance with the Guideline of the European Central Bank of 11th November 2010 on the legal framework for accounting and financial reporting in the European System of Central Banks (ECB/2010/20) and articles of Law on Bank of Slovenia that are applicable for financial reporting. This responsibility includes: designing, implementing and maintaining internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

Auditor's Responsibility
Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with International Standards on Auditing. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting

policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.
We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion
In our opinion, the financial statements give a true and fair view of the financial position of Bank of Slovenia as of December 31, 2010, and of its financial performance for the year then ended in accordance with the Guideline of the European Central Bank of 11th November 2010 on the Legal Framework for Accounting and Financial reporting in the European System of Central Banks (ECB/2010/20) and articles of Law on Bank of Slovenia, applicable for financial reporting.

DELOITTE REVIZIJA d.o.o.

Andreja Bajuk Mušič
Certified auditor
Andreja Bajuk M

Yuri Sidorovich
President of the board

Ljubljana, February 24th, 2011

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Ljubljana, Slovenija 1

Constitution

The Bank of Slovenia (the Bank) was constituted by the Law on the Bank of Slovenia dated 25 June 1991. The Bank is a legal entity, governed by public law, which independently disposes of its own property. The Bank is wholly owned by the state and is autonomous as regards its finances and administration. The Bank is supervised by Parliament. The Bank shall take care of the stability of domestic prices and of general liquidity of the financial system. According to the Bank of Slovenia Act (Official Gazette of the Republic of Slovenia No. 58/02 and No. 72/06), from the day of introduction of the euro, the Bank shall begin to perform the tasks in accordance with the Treaty establishing the European Community and in accordance with the Statute of the ESCB and the ECB[1].

Accounting policies

Introduction of euro

Republic of Slovenia introduced the euro as a new legal tender on the 1 January 2007. The Bank became part of the Eurosystem and took over joint responsibility for monetary policy and for exercising the common strategic goals of the European System of Central Banks (ESCB)[2].

Accounting principles and standards

The Bank applies the Guideline of the European Central Bank of 11 November 2010 on the legal framework for accounting and financial reporting in the European System of Central Banks (recast) (ECB/2010/20)[3] (Accounting Guideline) as the legal basis for the accounting and reporting. According to the Bank of Slovenia Act and according to the Statute of the ESCB and the ECB, this legal framework was adopted by the Governing Board of the Bank at its 343rd meeting on 20 December 2006.

Financial statements are presented in accordance with the valuation rules as defined by the Accounting Guideline.

In cases that are not covered by the Accounting Guideline or are governed by non-mandatory provisions, the valuation principles in accordance with International Financial Reporting Standards valid in EU and with the Bank of Slovenia act are applied.

Basic principles

The financial statements are prepared in conformity with the provisions governing the Eurosystem's accounting and reporting operations, which follow accounting principles, harmonized by Community law and generally accepted international accounting standards valid in EU and with the Bank of Slovenia act.

The following fundamental accounting principles have been applied:

- economic reality and transparency: the accounting methods and financial reporting shall reflect economic reality and shall be transparent;
- prudence: the valuation of assets and liabilities, as well as the recognition of income, shall be carried out prudently. In the context of the Accounting Guideline, this implies that unrealised gains are not recognised as income in the profit and loss account, but are transferred directly to a revaluation account;

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[1] Protocol (No. 18) (ex No. 3) on the Statute of the European System of Central Banks and of the European Central Bank (Protocol annexed to the Treaty establishing the European Community, OJ C 191, 29.07.1992).

[2] The term 'European System of Central Banks (ESCB)' refers to the twenty-seven National Central Banks (NCBs) of the member states of the European Union on 31 December 2010 plus the European Central Bank (ECB). The term 'Eurosystem' refers to the sixteen NCBs of the member states participating in the Monetary Union, plus the ECB on the same date.

[3] OJ L 35, 09.02.2011, p. 31-68.

* post-balance-sheet events: assets and liabilities shall be adjusted to take into account events that occur between the end of financial year and the date on which the annual accounts are approved by the Governing Board, if they materially affect the fair presentation of assets or liabilities at the balance sheet date;
* materiality: deviation from the accounting rules shall not be allowed unless they can reasonable be judged to be immaterial in the overall context and presentation of the financial statements;
* going concern basis: when assessing assets and liabilities, it must be assumed that the activities will continue;
* the accruals principle: income and expenditure shall be recognised in the accounting period they were earned or incurred, regardless of when the payment is made or received;
* consistency and comparability: the criteria for balance sheet valuation and income recognition shall be applied consistently to ensure comparability of data in the financial statements.

Recognition of assets and liabilities
An asset or liability is only recognised in the Balance Sheet when it is probable that any associated future economic benefit will flow to or from the Bank, substantially all of the associated risks and rewards have been transferred to the Bank, and the cost or value of the asset or the amount of the obligation can be measured reliably.

Economic approach
On the basis of definition of alternative economic approach in the Accounting Guideline, transactions in financial assets and liabilities are reflected during the year in the accounts on the basis of the date on which they were settled.

For transactions in foreign currency, agreed in one year but maturing in a subsequent year, the trade date approach is applied. Transactions are recorded in off-balance sheet accounts on the trade date. On the settlement date, the off-balance sheet entries are reversed and transactions are booked on-balance sheet. Purchases and sales of foreign currency affect the net foreign currency position on the trade date and realised results arising from sales are also calculated on the trade date.

Securities transactions are recorded according to the cash/settlement approach. Accrued interest, premiums and discounts related to financial instruments in foreign currency are calculated and booked daily from the settlement date, and the foreign currency position is also affected daily by these accruals.

Conversion of foreign currencies
Foreign currency transactions whose exchange rate is not fixed against the euro are recorded in the balance sheet at market rates prevailing on the day of the transaction. At year-end, both financial assets and liabilities are revalued at current market rates of the last day of the year, as derived from the ECB's daily quotation of reference exchange rates. This applies equally to on balance-sheet and off-balance-sheet transactions. The revaluation takes place on a currency-by-currency basis.

Income and expenses are converted at the exchange rate prevailing on the recording date.

Gold and gold receivables
Gold and gold receivables are valued at market price prevailing at the year-end. No distinction is made between the price and currency revaluation differences for gold. Instead, a single gold valuation is accounted for on a basis of the price in euro per fine ounce of gold, derived from the gold price in US dollar as at the balance sheet date.

Securities
Marketable securities (other than those classified as held-to-maturity) are valued at the market prices prevailing at the balance sheet date on a security-by-security basis. Investments in securities are included in the balance sheet items 'Claims on non-euro area residents denominated in foreign currency', 'Claims on euro area residents denominated in foreign currency', 'Claims on non-euro area residents denominated in euro', and 'Securities of euro area residents denominated in euro'.

Marketable securities classified as held-to-maturity, non-marketable securities and illiquid equity shares are valued at amortised cost and are subject to impairment.

Securities lending transactions under automated security lending contracts are concluded as part of the management of Bank's own assets. Securities lent by the Bank are collateralised. Income arising from lending operations is included in the profit and loss account. Automated security lending is conducted via agent and custodian banks. Transactions outstanding at year-end are recorded off-balance sheet.

Tangible fixed assets

Depreciation is calculated on a straight line basis, beginning in the month after acquisition so as to write off the cost of the assets over their estimated economic lifetime at the following annual percentage rates:

Buildings	1.3 – 1.8 %
Computers	20 – 33 %
Other equipment	10 – 25 %

Gains and losses on disposal of fixed assets are determined as the difference between net disposal proceeds and the carrying amount of the asset and are recognised as income or expense in the statement of income and expenditure.

Properties located in Austria are included in Bank's fixed assets. They are carried at fair value and are not depreciated. The fair value is demonstrated as half of appraisal value, obtained by an external certificated valuer (the Bank revalues these properties once every 5 years; the last revaluation was performed in year 2009). This revaluation method represents the deviation from generally accepted accounting principles. In its prudent concept it reduces the volatility of the financial statements.

ESCB capital key

The capital key is essentially a measure of the relative national size of EU member countries and is a 50:50 composite of GDP and population size. The key is used as the basis of allocation of each NCB's share capital in the ECB and must be adjusted every five years under ESCB statute and every time when a new country joins EU.

The Eurosystem key is an individual NCB's share of the total key held by Eurosystem members and is used as the basis for allocation of monetary income, banknotes in circulation, ECB's income on euro banknotes in circulation and the ECB's profit/loss.

Banknotes in circulation

The ECB and the sixteen euro area NCBs[4], which together comprise the Eurosystem, issue euro banknotes[5]. The total value of euro banknotes in circulation is allocated on the last working day of each month in accordance with the banknote allocation key[6].

The ECB has been allocated a share of 8% of the total value of euro banknotes in circulation, whereas the remaining 92% has been allocated to NCBs according to their weightings in the capital key of the ECB. The share of banknotes allocated to the Bank is disclosed under the liability balance sheet item 'Banknotes in circulation'.

The difference between the value of the euro banknotes allocated to each NCB in accordance with the banknote allocation key and the value of the euro banknotes that it actually puts into circulation also gives rise to remunerated intra-Eurosystem balances. These claims or liabilities, which incur interest[7],

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[4] Central bank of Estonia have only participated in the Eurosystem since 1st January 2011.

[5] Decision of the European Central Bank of 13 December 2010 on the issue of euro banknotes (recast) (ECB/2010/29), OJ L 35, 09.02.2011, p. 26-30.

[6] Banknote allocation key means the percentages that result from taking into account the ECB's share in the total euro banknote issue and applying the subscribed capital key to the NCBs' share in such total.

[7] Decision of the European Central Bank of 25 November 2010 on the allocation of monetary income of the national central banks of Member States whose currency is euro (recast) (ECB/2010/23), OJ L 35, 09.02.2011, p. 17-25.

are disclosed under the sub-item 'Net claims/liabilities related to the allocation of euro banknotes within the Eurosystem' (see 'Intra-ESCB balances' in the notes on accounting policies).

From the cash changeover year[8] until five years following the cash changeover year the intra-Eurosystem balances arising from the allocation of euro banknotes are adjusted (smoothing mechanism) in order to avoid significant changes in NCBs' relative income positions as compared to previous years. The adjustments are effected by taking into account the differences between the average value of banknotes in circulation of each NCB in the reference period[9] and the average value of banknotes that would have been allocated to them during that period under the ECB's capital key. The adjustments are reduced in annual stages until the first day of sixth year after the cash changeover year when income on banknotes is allocated fully in proportion to the NCBs' paid-up shares in the ECB's capital. For the Bank of Slovenia, the adjustment period will end on 31 December 2012. In the year under review the adjustments also resulted from the accession of Central Bank of Cyprus and Central Bank of Malta (in 2008) and Národná banka Slovenska (in 2009) and will terminate at the end of 2013 and 2014, respectively.

The interest income and expense on these balances is cleared through the accounts of the ECB and is disclosed under 'Net interest income' in the Profit and Loss account.

Interim profit distribution
The Governing Council of the ECB has decided that the seigniorage income of the ECB, which arises from the 8% share of euro banknotes allocated to the ECB, and the ECB's (net) income arising from SMP securities shall be due in full to the NCBs in the same financial year it accrues. The ECB shall distribute this income in January of the following year in the form of an interim distribution of profit[10]. The amount of the ECB's income on euro banknotes in circulation may be reduced in accordance with any decision by the Governing Council in respect of expenses incurred by the ECB in connection with the issue and handling of euro banknotes. Before the end of the year the Governing Council decides whether all or part of the ECB's income arising from SMP securities and, if necessary, all or part of the ECB's income on euro banknotes in circulation should be retained to the extent necessary to ensure that the amount of the distributed income does not exceed the ECB's net profit for that year.

The Governing Council may also decide to transfer all or part of the ECB's income arising from SMP securities and if necessary, all or part of the ECB's income on euro banknotes in circulation to a provision for foreign exchange rate, interest rate, credit and gold price risks. The amount distributed to NCBs is disclosed in the Profit and Loss account under 'Income from equity shares and participating interest'.

Provisions
Provisions for legal claims are recognised when the Bank has a present legal or constructive obligation as a result of past events, when: it is more likely than not that an outflow of resources will be required to settle the obligation; and the amount can be reliably estimated.

In compliance with Article 49a of Bank of Slovenia Act, after introduction of the euro as the Republic of Slovenia's currency, the Governing Board of the Bank may, with the intention of maintaining the real value of assets, take a decision to create provisions for anticipated exchange rate, interest rate and price risks. Provisions may not be created if, together with the unrealised exchange rate differences, securities' valuation effects and gold valuation effects, they exceed 20% of established net income. The relevant amount of provision for such risks is determined annually on the basis of Value-at-Risk (VaR) method. VaR is defined as the maximum loss of portfolio with a given diversification of that

[8] Cash changeover year refers to the year in which the euro banknotes are introduced as legal tender in the respective Member State, for Bank of Slovenia this is 2007.

[9] The reference period refers to the 24 months which start 30 months before the day on which euro banknotes become legal tender in the respective Member State, for Bank of Slovenia this is the period from July 2004 to June 2006.

[10] Decision of the European Central Bank of 25 November 2010 on the interim distribution of the income of the European Central Bank on euro banknotes in circulation and arising from securities purchased under the securities markets programme (ECB/2010/24), OJ L 6, 11.01.2011, p. 35-36.

portfolio at a certain level of probability (95%) and for a given holding period (one year). The provision will be used to fund future unrealised losses not covered by the revaluation accounts.

Intra-ESCB balances
Intra-ESCB transactions are cross-border transactions that occur between two ESCB central banks. These transactions are processed primarily via TARGET2[11] and give rise to the daily net bilateral position. This position in the books of the Bank represents the net claim or liability of the Bank against the rest of the ESCB members connected to TARGET2.

Intra-Eurosystem balances arising from the allocation of euro banknotes within the Eurosystem are included as a net single asset under 'Net claims related to the allocation of euro banknotes within the Eurosystem' (see 'Banknotes in circulation' in the Accounting policies).

Income recognition
Income and expenses are recognised in the financial year in which they are earned or incurred. Realised gains and losses are taken to the Profit and Loss account.

From the beginning of 2007, the foreign exchange and price valuation is performed on a quarterly basis in accordance with the Accounting Guideline. Net unrealised valuation gains which arose before the euro adoption are separated from the unrealised valuation gains recorded after that date. They are considered as a 'pre-Stage Three' revaluation reserves and are included into the liability balance sheet item 'Reserves'.

At the end of year, unrealised gains are not recognised as income in the Profit and Loss account but are recorded on the revaluation accounts on the liabilities side of the balance sheet.

Unrealised losses are taken to the Profit and Loss account if they exceed previous revaluation gains registered in the corresponding revaluation account. Such losses can not be reversed against any future unrealised gains in subsequent years. Unrealised gains and losses in respect of securities and foreign currency denominated items are entered on an item-by-item basis and a currency-by-currency basis. Netting is not allowed.

Premiums and discounts arising on purchased securities are calculated and presented as part of interest income and are amortised over the remaining life of the security according to the internal rate of return (IRR) method.

Cost of transactions
With regard to gold, foreign currencies and securities, the average cost method as defined in the Accounting Guideline is used daily to establish the acquisition cost of items sold when calculating effects of exchange rates and prices.

When net acquisitions of currency (or gold) are made, the average acquisition cost for the day's acquisition with regard to each individual currency is added to the previous day's holdings to obtain a new weighted average of the exchange rate (or gold price) respectively. In case of net sales, the realised result is calculated on the basis of the average acquisition cost of the previous day for the respective foreign currency position.

Gains and losses on disposals of securities are calculated on the basis of the weighted average price of individual security.

The market prices and rates applied in the opening balance sheet as at 1 January 2007 were considered as the opening average cost of Bank's assets and liabilities. In case of foreign currency positions and gold, the opening costs were the exchange rates prevailing on 1 January 2007, communicated by the ECB. For securities investments, the securities prices as at 31 December 2006 represented the opening average prices, which served as a starting-point for premium and discount amortisation and calculation of realised gains and losses in case of their sale.

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[11] Trans-European Automated Real-time Gross settlement Express Transfer system 2

Off-balance-sheet instruments
Forward legs of foreign exchange swaps are disclosed off-balance-sheet and are included in the net foreign currency position for the purpose of calculating the average cost of currencies and foreign exchange gains and losses. Gains and losses arising from the forward legs are recognised and treated in a similar manner to on-balance sheet instruments. Unrealised valuation gains are not recognised as income but are transferred to the revaluation accounts. Unrealised valuation losses are taken to the Profit and Loss account when exceeding previous revaluation gains registered in the revaluation accounts. Unrealised valuation gains/losses of the forward legs of foreign exchange swaps are recorded from the trade date to the settlement date under 'Other assets/liabilities'.

Since spot and forward amounts in foreign currencies are converted to euro at the same exchange rate, foreign exchange swaps do not influence Profit and Loss accounts or the revaluation accounts on the liabilities side.

Post-balance-sheet events
Assets and liabilities are adjusted for events that occur between the annual balance sheet date and the date on which the Governing Board approves the financial statements, if such events materially affect the condition of assets and liabilities on the balance sheet date.

On 1 January 2011, Estonia adopted euro as a new legal tender and paid up its capital share to the ECB in full. As a result, the Bank's share in the fully paid-up capital of the ECB decreased from 0,4711% to 0,4699% on 1 January 2011.

Cash flow statement
Taking account of the Bank's role as a central bank, the publication of a cash flow statement would not provide the readers of the financial statements with any additional relevant information. Therefore, such a statement is not included as part of these statements.

Taxation
The Bank is not subject to Slovenian corporate income tax.

Appropriations
In accordance with the Bank of Slovenia Act, net profit is allocated to general reserves and the Budget of the Republic of Slovenia. Unrealised income deriving from exchange rate and price changes is allocated in its entirety to the revaluation accounts and it is not included in a net profit available for distribution. Revaluation accounts may only be used to cover a shortfall deriving from unrealised losses as a result of exchange rate and price movements.

A net loss of the Bank is covered from general reserves. In case that the net loss arises from unrealised exchange rate and price changes, it shall be covered from the special reserves created for that purpose. Any net loss which cannot be covered from general reserves is covered by the budget of the Republic of Slovenia.

Auditing of financial statements
The financial statements were audited by Deloitte revizija d.o.o., Ljubljana, who was appointed as the external auditor of the Bank for the financial years 2009 to 2011.

Balance Sheet as at 31 December 2010

ASSETS (thousands of euro)		31 December 2010	31 December 2009
1	**Gold and gold receivables**	**108,005**	**78,428**
2	**Claims on non-euro area residents denominated in foreign currency**	**691,714**	**672,425**
	2.1 Receivables from the IMF	315,306	261,512
	2.2 Balances with banks and security investments, external loans and other external assets	376,408	410,913
3	**Claims on euro area residents denominated in foreign currency**	**259,369**	**245,136**
4	**Claims on non-euro area residents denominated in euro**	**767,535**	**877,855**
	4.1 Balances with banks, security investments and loans	767,535	877,855
	4.2 Claims arising from the credit facility under ERM II	-	-
5	**Lending to euro area credit institutions related to monetary policy operations denominated in euro**	**602,000**	**2,114,800**
	5.1 Main refinancing operation	53,000	1,000
	5.2 Longer-term refinancing operations	539,000	2,113,800
	5.3 Fine-tuning reverse operations	10,000	-
	5.4 Structural reverse operations	-	-
	5.5 Marginal lending facility	-	-
	5.6 Credits related to margin calls	-	-
6	**Other claims on euro area credit institutions denominated in euro**	**94,954**	**19,878**
7	**Securities of euro area residents denominated in euro**	**3,096,428**	**2,941,945**
	7.1 Securities held for monetary policy purposes	668,500	84,703
	7.2 Other securities	2,427,928	2,857,242
8	**General government debt denominated in euro**	**-**	**-**
9	**Intra-Eurosystem claims**	**2,727,519**	**2,752,257**
	9.1 Participating interest in ECB	63,820	58,340
	9.2 Claims equivalent to the transfer of foreign reserves	189,410	189,410
	9.3 Claims related to promissory notes backing the issuance of ECB debt certificates*	-	-
	9.4 Net claims related to the allocation of euro banknotes within the Eurosystem	2,474,289	2,504,507
	9.5 Other claims within the Eurosystem (net)	-	-
10	**Items in course of settlement**	**-**	**-**
11	**Other assets**	**213,728**	**284,537**
	11.1 Coins of euro area	2,149	1,654
	11.2 Tangible and intangible fixed assets	22,336	21,136
	11.3 Other financial assets	56,396	50,426
	11.4 Off-balance sheet instruments revaluation differences	242	809
	11.5 Accruals and prepaid expenses	73,141	71,574
	11.6 Sundry	59,463	138,937
12	**Loss for the year**	**-**	**-**
Total assets		**8,561,253**	**9,987,259**

* Only an ECB balance sheet item

LIABILITIES (thousands of euro)	31 December 2010	31 December 2009
1 Banknotes in circulation	**3,640,108**	**3,495,792**
2 Liabilities to euro area credit institutions related to monetary policy operations denominated in euro	**882,037**	**1,220,232**
2.1 Current accounts (covering the minimum reserve system)	442,137	415,132
2.2 Deposit facility	304,900	805,100
2.3 Fixed-term deposits	135,000	-
2.4 Fine-tuning reverse operations	-	-
2.5 Deposits related to margin calls	-	-
3 Other liabilities to euro area credit institutions denominated in euro	**14,191**	**13,655**
4 Debt certificates issued	**-**	**-**
5 Liabilities to other euro area residents denominated in euro	**288,298**	**299,943**
5.1 General government	269,821	270,725
5.2 Other liabilities	18,476	29,217
6 Liabilities to non-euro area residents denominated in euro	**33,368**	**16,174**
7 Liabilities to euro area residents denominated in foreign currency	**75,639**	**68,743**
8 Liabilities to non-euro area residents denominated in foreign currency	**-**	**-**
8.1 Deposits, balances and other liabilities	-	-
8.2 Liabilities arising from the credit facility under ERM II	-	-
9 Counterpart of special drawing rights allocated by the IMF	**249,818**	**235,009**
10 Intra-Eurosystem liabilities	**2,092,831**	**3,333,973**
10.1 Liabilities equivalent to the transfer of foreign reserves*	-	-
10.2 Liabilities related to promissory notes backing the issuance of ECB debt certificates	-	-
10.3 Net liabilities related to the allocation of euro banknotes within the Eurosystem	-	-
10.4 Other liabilities within the Eurosystem (net)	2,092,831	3,333,973
11 Items in course of settlement	**-**	**-**
12 Other liabilities	**112,779**	**189,905**
12.1 Off-balance sheet instruments revaluation differences	23,999	7,295
12.2 Accruals and income collected in advance	5,385	6,690
12.3 Sundry	83,395	175,920
13 Provisions	**143,905**	**118,538**
14 Revaluation accounts	**188,068**	**167,378**
15 Capital and reserves	**802,027**	**724,352**
15.1 Capital	8,346	8,346
15.2 Reserves	793,681	716,007
16 Profit for the year	**38,184**	**103,566**
Total liabilities	**8,561,253**	**9,987,259**

* Only an ECB balance sheet item

Profit and Loss Account for the year ended 31 December 2010

thousands of euro	2010	2009
1.1 Interest income	145,458	170,519
1.2 Interest expense	-42,864	-53,680
1 Net interest income (expenditure)	**102,594**	**116,840**
2.1 Realised gains/losses arising from financial operations	31,208	62,787
2.2 Write-downs on financial assets and positions	-59,087	-15,113
2.3 Transfer to/from provisions for foreign exchange risks, price risks and other operational risks	-33,635	-64,894
2 Net result of financial operations, write-downs and risk provisions	**-61,514**	**-17,220**
3.1 Fee and commission income	7,434	12,028
3.2 Fee and commission expense	-1,698	-1,556
3 Net fee and commission income	**5,736**	**10,471**
4 Income from equity shares and participating interests	7,844	4,128
5 Net result arising from allocation of monetary income	8,071	14,848
6 Other operating income	4,140	4,195
Total net income	**66,871**	**133,262**
7.1 Staff costs	-18,644	-17,989
7.2 Administrative expenses	-5,890	-6,981
7.3 Depreciation of tangible and intangible fixed assets	-1,946	-2,108
7.4 Banknote production services	-1,679	-2,166
7.5 Other expenses	-528	-452
7 Total operating expenses	**-28,687**	**-29,696**
8 Profit (Loss) for the year	**38,184**	**103,566**

The notes on pages 14 to 32 form an integral part of the financial statements.

The unaudited financial statements were approved by the Governing Board on 15 February 2011 and these audited financial statements were approved by the Governing Board on 15 March 2011 and were signed on its behalf by:

Marko Kranjec, Ph. D.
President of the Governing Board and
Governor of the Bank of Slovenia

In accordance with Article 49 of the Bank of Slovenia Act, the Bank of Slovenia shall inform the National Assembly of the Republic of Slovenia of these annual financial statements.

Notes to the balance sheet

Assets

1. Gold and gold receivables

With the exception of gold stocks held in the Bank, the Bank's gold holdings consist of deposits with foreign banks. In the annual accounts gold has been valued on the basis of the euro price per fine ounce (ozf) derived from the quotation in USD established at the London fixing on 31 December 2010. This price, notified by the ECB, amounts to EUR 1,055.418 per ounce of fine gold compared with EUR 766.347 on 31 December 2009. Unrealised valuation gains of EUR 58.6 million (of which EUR 8.8 million from year 2007, EUR 5.5 million from year 2008, EUR 14.8 million from year 2009 and EUR 29.6 million from year 2010) were disclosed under the liability balance sheet item 'Revaluation accounts'.

	000 EUR	Fine troy ounces
Balance as at 31 December 2009	78,428	102,014
Revaluation of gold stock as at end of 2010	29,578	-
Balance as at 31 December 2010	108,005	102,334

2. Claims on non-euro area residents denominated in foreign currency

This item includes holdings of Special Drawing Rights (SDRs) allocated by the International Monetary Fund (IMF) and foreign currency claims on non-euro area residents included in the Bank's foreign reserves.

The sub-item 2.1 'Receivables from the IMF' consists of drawing rights within the reserve tranche and special drawing rights. They are remunerated by the IMF at a remuneration rate that is updated weekly.

The reserve tranche corresponds to the difference between Slovenian's quota in the IMF and the IMF's holdings of EUR with the Bank. The tranche is usually used for the purpose of financing the balance of payments deficit in the member countries.

Loans to the IMF are based on the loan agreement between the Bank and IMF, dated 1 September 2010. Borrowed funds give IMF the possibility to ensure timeliness and effective assistance to the member countries in case of balance of payments difficulties.

SDRs are reserve assets created by the IMF and allocated by it to its members in order to increase international liquidity. They are used in transactions between official monetary authorities. The SDR is defined in terms of a basket of currencies. Its value is determined as the weighted sum of exchange rates of four currencies (USD, GBP, JPY and EUR).

Both claims are shown in the balance sheet on the basis of the market rate of SDR 1 = EUR 1.1572 (31 December 2009: SDR 1 = EUR 1.0886) calculated by the ECB at the end of the year for all central banks participating in the Eurosystem. At the balance sheet date, the market rate of SDR was below the average cost and valuation losses were therefore recognised in accordance with the accounting rules in the Profit and Loss Account.

	31 December 2010		31 December 2009	
	000 SDR	000 EUR	000 SDR	000 EUR
Quota	231,700	268,123	231,700	252,229
Less IMF holdings of EUR	-180,607	-208,998	-189,607	-206,406
Reserve tranche in the IMF	51,093	59,125	42,093	45,823
Loan to the IMF	23,200	26,847	-	-
SDR Holdings	198,180	229,334	198,134	215,689
Total	272,473	315,306	240,227	261,512

The sub-item 2.2 'Balances with banks and security investments, external loans and other external assets' includes the foreign currency assets held with non-euro area residents (including international and supranational organisations). Foreign currency assets are shown under this sub-item at their euro equivalent as calculated on the basis of market exchange rates on 31 December 2010.

Breakdown of foreign currency assets by type of investment:

	31 December 2010	31 December 2009
	000 EUR	000 EUR
Current accounts	1,020	1,301
Time deposits	58,374	51,367
Securities	317,014	358,245
Total	376,408	410,913

Breakdown of foreign currency assets by currency:

	31.12.2010	31.12.2009
	000 EUR	000 EUR
USD	294,252	277,807
AUD	75,668	98,846
GBP	5,889	33,908
Other currencies	599	352
Total	376,408	410,913

Breakdown of securities according to their residual maturity:

	31 December 2010	31 December 2009
	000 EUR	000 EUR
≤ 1 year	133,045	135,800
>1 year and ≤5 years	176,163	222,444
> 5 years	7,805	-
Total	317,014	358,245

3. Claims on euro area residents denominated in foreign currency

The foreign currency assets held with euro area residents are invested in sight deposits, time deposits and securities in foreign currencies. Foreign currency assets are shown at their euro equivalent as calculated on basis of market exchange rates on 31 December 2010.

Breakdown of foreign currency assets by type of investment:

	31 December 2010	31 December 2009
	000 EUR	000 EUR
Current accounts	179	117
Time deposits	17,213	-
Securities	241,978	245,019
Total	259,369	245,136

Breakdown of foreign currency assets by currency:

	31.12.2010	31.12.2009
	000 EUR	000 EUR
USD	236,173	214,825
AUD	11,510	18,719
GBP	11,684	11,592
Other currencies	-	-
Total	259,369	245,136

Breakdown of securities according to their residual maturity:

	31 December 2010	31 December 2009
	000 EUR	000 EUR
≤ 1 year	77,953	86,281
>1 year and ≤ 5 years	164,025	158,738
> 5 years	-	-
Total	241,978	245,019

4. Claims on non-euro area residents denominated in euro

The claims on non-euro area residents denominated in euro included under this balance sheet item are invested in sight deposits, time deposits and securities.

Breakdown of euro denominated assets by type of investment:

	31 December 2010	31 December 2009
	000 EUR	000 EUR
Current accounts	1,956	812
Time deposits	-	142,331
Securities	765,579	734,711
Total	767,535	877,855

Breakdown of securities according to their residual maturity:

	31 December 2010	31 December 2009
	000 EUR	000 EUR
≤ 1 year	124,339	138,118
>1 year and ≤ 5 years	559,775	470,769
> 5 years	81,465	125,825
Total	765,579	734,711

5. Lending to euro area credit institutions related to monetary policy operations in euro

This item shows operations carried out by the Bank within the framework of the single monetary policy of the Eurosystem and reflects the volume and pattern of the Bank's refinancing of the Slovenian credit institutions.

The total Eurosystem holding of monetary policy assets amounts to EUR 546,747 million, of which the Bank holds EUR 602 million. In accordance with Article 32.4 of the Statute, any risks from monetary policy operations, if they were to materialise, should eventually be shared in full by the Eurosystem NCBs, in proportion to the prevailing ECB capital key shares.

Main refinancing operations are regular liquidity-providing operations which are conducted with a weekly frequency in the form of reverse transactions and executed through standard tenders. In 2010 the main refinancing operations were conducted as fixed rate tender procedures with full allotment. As a main monetary policy instrument, they play a pivotal role in fulfilling the objectives of Eurosystem's market operations.

Longer-term refinancing operations are regular liquidity-providing reverse transactions with a maturity of one, three, six or twelve months. In the year under review longer-term refinancing operations provided the bulk of refinancing to the banking sector. They were conducted as fixed rate tender procedures with full allotment. For some operations the rate was fixed at the average minimum bid rate of the MROs over the life of this operation. At the end of year 2010, only one- and three- months operations existed, conducted with a monthly frequency.

Fine-tuning reverse operations are not conducted regularly by the ECB. They were performed four times in 2010 at the maturity of six- and twelve- months longer-term refinancing operations with the aim to overcome the liquidity until the subsequent main refinancing operation. Maturity of these transactions was between 6 and 13 days. They were conducted as fixed rate tenders with full allotment.

	31 December 2010	31 December 2009
	000 EUR	000 EUR
Main refinancing operations	53,000	1,000
Longer term refinancing operations	539,000	2,113,800
Fine-tuning reverse operations	10,000	-
Total	602,000	2,114,800

6. Other claims on euro area credit institutions denominated in euro

This item comprises claims on credit institutions which do not relate to monetary policy operations. Claims consist almost entirely of fixed-term euro-denominated deposits which are held at euro area credit institutions.

	31 December 2010	31 December 2009
	000 EUR	000 EUR
Current accounts	1,585	1,578
Time deposits	93,369	18,300
Total	94,954	19,878

7. Securities of euro area residents denominated in euro

This item includes securities held for monetary policy purposes and other securities issued by euro area residents denominated in euro.

The sub-item 7.1 'Securities held for monetary policy purposes' contains securities acquired by the Bank within the scope of the purchase programme for covered bonds[12], and public debt securities acquired in the scope of the securities market programme[13]. The securities are classified as held-to-maturity.

The total Eurosystem NCB's holding of SMP securities amounts to EUR 73,976 million, of which the Bank holds EUR 402 million. In accordance with Article 32.4 of the Statute, any risks from monetary policy operations, if they were to materialise, should eventually be shared in full by the Eurosystem NCBs, in proportion to the prevailing ECB capital key shares.

Breakdown of securities held for monetary policy purposes according to their residual maturity:

	31 December 2010	31 December 2009
	000 EUR	000 EUR
≤ 1 year	96,012	-
>1 year and ≤ 5 years	411,316	77,285
> 5 years	161,173	7,418
Total	668,500	84,703

The sub-item 7.2 'Other securities' covers the portfolio of marketable securities, issued by governments and credit institutions of the euro area.

Breakdown of other securities according to their residual maturity:

	31 December 2010	31 December 2009
	000 EUR	000 EUR
≤ 1 year	610,523	744,735
>1 year and ≤ 5 years	1,695,261	2,000,545
> 5 years	122,144	111,962
Total	2,427,928	2,857,242

[12] Decision of the European Central Bank of 2 July 2009 on the implementation of the covered bond purchase programme (ECB/2009/16), OJ L 175, 04.07.2009, p. 18-19.

[13] Decision of the European Central Bank of 14 May 2010 establishing a securities markets programme (ECB/2010/5), OJ L 124, 20.05.2010, p. 8-9.

9. Intra-Eurosystem claims

Sub-item 9.1 shows the Bank's participating interest in the ECB. Pursuant to Article 28 of the Statute of the ESCB and the ECB, the ESCB national central banks are the sole subscribers to the capital of the ECB. Subscriptions depend on shares which are fixed in accordance with Article 29.3 of the Statute and which must be adjusted every five years. The most recent such adjustment took effect on 1 January 2009.

The ECB increased its subscribed capital by EUR 5,000 million from EUR 5,760,652,402.58 to EUR 10,760,652,402.58 with effect from 29 December 2010. The NCBs of the euro area countries shall pay up their increased capital in three equal annual instalments. The first instalment was paid on 29 December 2010, and the following instalments shall be paid at the end of 2011 and 2012. Consequently, on 29 December Banka Slovenije paid EUR 5,480,000 as its first instalment.

The subscribed and paid up capital of the 27 European central banks in the capital of the ECB on 31 December 2010 is as follows:

	Capital key per cent	EUR	Of which fully paid up	Eurosystem key
Nationale Bank van België/ Banque Nationale de Belgique	2.4256	261,010,385	180,157,051	3.4755
Deutsche Bundesbank	18.9373	2,037,777,027	1,406,533,694	27.1341
Central Bank and Financial Services Authority of Ireland	1.1107	119,518,566	82,495,233	1.5914
Bank of Greece	1.9649	211,436,059	145,939,392	2.8154
Banco de España	8.3040	893,564,576	616,764,576	11.8983
Banque de France	14.2212	1,530,293,899	1,056,253,899	20.3767
Banca d'Italia	12.4966	1,344,715,688	928,162,355	17.9056
Central Bank of Cyprus	0.1369	14,731,333	10,168,000	0.1962
Banque centrale du Luxembourg	0.1747	18,798,860	12,975,526	0.2503
Central Bank of Malta/Bank Ĉentrali ta' Malta	0.0632	6,800,732	4,694,066	0.0906
De Nederlandsche Bank	3.9882	429,156,339	296,216,339	5.7144
Oesterreichische Nationalbank	1.9417	208,939,588	144,216,254	2.7821
Banco de Portugal	1.7504	188,354,460	130,007,793	2.5080
Banka Slovenije	**0.3288**	**35,381,025**	**24,421,025**	**0.4711**
Národná banka Slovenska	0.6934	74,614,364	51,501,030	0.9935
Suomen Pankki-Finlands Bank	1.2539	134,927,820	93,131,154	1.7966
Total euro-area NCBs	**69.7915**	**7,510,020,722**	**5,183,637,388**	**100.0000**
Bulgarian National Bank	0.8686	93,467,027	3,505,014	
Česká národní banka	1.4472	155,728,162	5,839,806	
Danmarks Nationalbank	1.4835	159,634,278	5,986,285	
Eesti Pank	0.1790	19,261,568	722,309	
Latvijas Banka	0.2837	30,527,971	1,144,799	
Lietuvos bankas	0.4256	45,797,337	1,717,400	
Magyar Nemzeti Bank	1.3856	149,099,600	5,591,235	
Narodowy Bank Polski	4.8954	526,776,978	19,754,137	
Banca Naţională a României	2.4645	265,196,278	9,944,860	
Sveriges Riksbank	2.2582	242,997,053	9,112,389	
Bank of England	14.5172	1,562,145,431	58,580,454	
Total non-euro area NCBs	**30.2085**	**3,250,631,681**	**121,898,688**	
Total euro area and non-euro area NCBs	**100.0000**	**10,760,652,403**	**5,305,536,076**	

In accordance with Article 49.2 of the Statute of the ESCB and the ECB and the legal acts adopted by the Governing Council of the ECB, the Bank also made a contribution in year 2007 of EUR 36.7 million to the ECB's foreign exchange, gold and security price revaluation accounts and to the ECB's provision for foreign exchange rate, interest rate and gold price risks. The payment was made in two parts. As a result of a difference between the euro equivalent of FX reserves to be transferred to the ECB at current exchange rates and the claim of the Bank in accordance with its capital key (disclosed under asset item 9.2), the amount of EUR 7.6 million was used as the advance contribution to the ECB reserves, provisions and provisions equivalent to reserves on 3 January 2007. The rest of the contribution was paid after the approval of the ECB 2006 Annual Accounts by the Governing Council of the ECB in March 2007.

Due to a change in the ECB's capital key on 1 January 2009, the additional contribution to the ECB's net equity was made on 9 March 2009.

	31 December 2010
	000 EUR
Contribution to revaluation accounts	
- paid on 3 January 2007	7,647
- paid on 12 March 2007	18,105
Contribution to provisions	
- paid on 12 march 2007	10,947
Contribution paid on 9 March 2009	2,700
Total	39,399

Sub-item 9.2 contains the Bank's claims arising from the transfer of foreign reserve assets to the ECB. The claims are denominated in euro at a value fixed at the time of their transfer. They are remunerated at the latest available marginal rate for the Eurosystem's main refinancing operations, adjusted to reflect a zero return on the gold component.

Sub-item 9.4 'Net claims related to the allocation of euro banknotes within the Eurosystem' consists of the claims and liabilities of the Bank vis-à-vis the Eurosystem relating to the allocation of euro banknotes within the Eurosystem which arise from applying the euro banknote allocation key (see 'Banknotes in circulation' and 'Intra-ESCB balances' in the notes on accounting policies)[14]. The net position, taking into account the adjustment as a result of smoothing mechanism, which reduces the interest bearing claim for the compensatory amount of EUR 877.7 million (2009: EUR 1,155.0 million), is remunerated at the marginal interest rate applying to the main refinancing operations.

11. Other assets

The Bank's holding of coins, issued by Republic of Slovenia, are shown in sub-item 11.1 'Coins of euro area'.

Sub-item 11.2 'Tangible and intangible fixed assets' comprises land and buildings, computer hardware and software, furniture and other equipment.

[14] According to the accounting regime chosen by the Eurosystem on the issue of euro banknotes, a share of 8% of the total value of the euro banknotes in circulation is allocated to the ECB on a monthly basis. The remaining 92% of the value of the euro banknotes in circulation are allocated to the NCBs also on a monthly basis, whereby each NCB shows in its balance sheet a share of the euro banknotes issued corresponding to its paid-up share in the ECB's capital. The difference between the value of the euro banknotes allocated to the NCB according to the aforementioned accounting regime, and the value of euro banknotes put into circulation, is recorded as a 'Net Intra-Eurosystem claim/liability related to the allocation of euro banknotes within the Eurosystem'.

	Land and buildings	Computers & equipment	Total
	000 EUR	000 EUR	000 EUR
Cost or valuation			
At 31 December 2009	**20,272**	**19,203**	**39,476**
Additions	1,832	1,344	3,176
Disposals	-	624	624
At 31 December 2010	**22,104**	**19,923**	**42,028**
Depreciation			
At 31 December 2009	**3,328**	**15,011**	**18,339**
Disposals	0	622	622
Charge for the year	163	1,811	1,974
At 31 December 2010	**3,491**	**16,201**	**19,692**
Net book value			
At 31 December 2009	**16,944**	**4,192**	**21,136**
At 31 December 2010	**18,613**	**3,723**	**22,336**

As at 31 December 2010 an amount of EUR 8.0 million relating to investment properties in Austria is included in land and buildings (2009: EUR 8.0 million).

Sub-item 11.3 'Other financial assets' contains the Bank's participating interests in international financial organisations and other financial assets.

Sub-item 11.4 'Off-balance sheet instruments revaluation differences' includes the positive revaluation effect arising from the forward legs of foreign currency swaps, which are recorded on off-balance-sheet account.

Sub-item 11.5 'Accruals and prepaid expenses' contains the accrued income identified at 31 December 2010. This consists mainly of interest income which is due in the new financial year.

Sub-item 11.6 'Sundry' consists of fiduciary and other assets.

Liabilities

1. Banknotes in circulation

This item consists of the Bank's share of the total euro banknotes in circulation (see 'Banknotes in circulation' in the notes on accounting policies).

The total value of euro banknotes issued by the central banks in the Eurosystem is distributed among these banks on the last day of each month in accordance with the key for allocating euro banknotes (see Accounting policies). In accordance with the banknote allocation key applying on 31 December 2010, the Bank has a 0.4335% (2009: 0.4335%) share of the value of all euro banknotes in circulation. During the year 2010 the total value of banknotes in circulation within the Eurosystem rose from EUR 806,522 million to EUR 839,702 million. In accordance with the allocation key, the Bank shows holdings of euro banknotes amounting to EUR 3,640.1 million at the end of the year 2010 (2009: EUR 3,495.8 million). The value of the euro banknotes actually issued by the Bank was EUR 1,165.8 million (2009: EUR 991.3 million). As this was less that the allocated amount, the difference of EUR 2,474.3 million (2009: EUR 2,504.5 million) is shown in asset sub-item 9.4 'Net claims related to the allocation of euro banknotes within the Eurosystem'.

	31 December 2010	31 December 2009
	000 EUR	000 EUR
EUR 5	-9,819	-5,365
EUR 10	148,319	92,037
EUR 20	2,391,334	1,856,397
EUR 50	-1,360,001	-1,112,589
EUR 100	-215,193	-116,745
EUR 200	-103,813	-72,140
EUR 500	314,993	349,689
Total euro banknotes actually put into circulation by the Bank	1,165,819	991,285
Redistribution of euro banknotes in circulation within the Eurosystem	2,790,767	2,808,438
Euro banknotes issued by the ECB (8%)	-316,479	-303,931
Total EUR banknotes according to the Bank's banknote allocation key	3,640,108	3,495,792

2. Liabilities to euro area credit institutions related to monetary policy operations denominated in euro

These interest bearing liabilities arise from the monetary policy conducted by the Bank on behalf of the ESCB.

Sub-item 2.1 'Current accounts' contains the deposits of credit institutions, which are used to meet the minimum reserve requirements and to settle payments. The main criterion for including these deposits in this sub-item is that the respective institution is subject to the Eurosystem minimum reserve system. Reserve requirements have to be fulfilled on average over the reserve maintenance period, which lasts approximately one month, in accordance with the schedule published by the ECB. Banks' reserve balances up to calculated reserve requirements have been remunerated on a daily basis at the prevailing interest rate for the Eurosystem's main refinancing operations.

Sub-item 2.2 'Deposit facility' contains overnight deposits placed with the Bank by slovenian counterparties at a predetermined interest rate (standing facility).

Sub-item 2.3 'Fixed term deposits' contains operations, performed by the ECB usually on the last day of the reserve maintenance period. Maturity of these operations is one day; they are conducted as variable rate tenders. Since the establishment of the securities markets programme in May 2010, also fixed term deposit operations are conducted with a weekly frequency and maturity of one week, with the aim to sterilise liquidity issued using this programme. Fixed term deposit operations are conducted as variable rate tenders.

	31 December 2010	31 December 2009
	000 EUR	000 EUR
Current accounts (covering the minimum reserve system)	442,137	415,132
Deposit facility	304,900	805,100
Fixed term deposits	135,000	-
Total	882,037	1,220,232

3. Other liabilities to euro area credit institutions denominated in euro

This balance sheet item contains other credit institutions' accounts unrelated to the monetary policy operations.

5. Liabilities to other euro area residents denominated in euro

Sub-item 5.1 'General government' encompasses the balances of the government sight and fixed-term deposits and its special funds in euro. The deposits of other public depositors constitute balances held by local communities.

Sub-item 5.2 Other liabilities' includes among other also stock exchange market customers' accounts and fixed term deposit of Guarantee fund of Central Securities Clearing Corporation.

6. Liabilities to non-euro area residents denominated in euro

Balance sheet item 'Liabilities to non-euro area residents denominated in euro' contains euro balances of international and supranational organisations and non-Eurosystem central banks. The IMF account No. 2 is also included in this balance sheet item.

7. Liabilities to euro area residents denominated in foreign currency

This item contains the foreign currency sight and fixed-term deposits of central government and its special funds.

9. Counterpart of special drawing rights allocated by the IMF

This item represents the liability of the Bank towards IMF which corresponds to the allocation of SDRs to the Republic of Slovenia as a result of its membership in the IMF. The liability is shown in the balance sheet at the end of 2010 on the basis of the market rate of SDR 1 = EUR 1.1572 (31 December 2009: SDR 1 = EUR 1. 0886) calculated by the ECB at the end of the year for all central banks participating in the Eurosystem. The increase in the amount of this liability in 2010 is solely due to valuation effects, i.e. the depreciation of the euro against the SDR.

10. Intra-Eurosystem liabilities

Sub-item 10.4 'Other liabilities within the Eurosystem (net)' includes net position of 'Other claims/liabilities within the Eurosystem (net). This item consists of a net TARGET2 balance, arising from cross-border transfers via TARGET2 with other NCBs in the ESCB and the ECB, the claim/liability arising from the allocation of monetary income to the national central banks (see profit and loss item 5 'Net result arising from allocation of monetary income') and the claim arising from the distribution of ECB's income on euro banknotes in circulation (see profit and loss item 4 'Income from equity shares and participating interests').

The net TARGET2 balance is remunerated at the latest available marginal rate for the main refinancing operations. The settlement takes place monthly on the second business day of the month following that to which the interest relates. The creation of this liability reflects outflows of funds from domestic credit institutions to other euro area countries. These funds came from the gradual release of credit institutions' deposits with the Bank after Slovenia joined EMU on 1 January 2007.

12. Other liabilities

Sub-item 12.1 'Off-balance sheet instruments revaluation differences' includes the negative revaluation effect arising from the forward legs of foreign currency swaps, which are recorded on off-balance-sheet account.

Sub-item 12.2 'Accruals and income collected in advance' contains the accrued expenses identified at 31 December 2010. This consists mainly of interest expenditure which is due in the new financial year but was incurred in the financial year just ended.

Sub-item 12.3 'Sundry' consists mainly of fiduciary liabilities and non-returned tolar banknotes.

13. Provisions

	31 December 2010	31 December 2009
	000 EUR	000 EUR
Provisions for employees and for known risks	80,654	80,119
Provisions for general risks	53,137	20,037
Provision in respect of monetary policy operations	10,114	18,381
Total	143,905	118,538

Provisions for employees and for known risks

Provisions for post-employment benefits are calculated in accordance with IAS 19 – Employee benefits on the basis of actuarial assumptions as at 31.12.2006. The latter consider the stipulations of the Bank collective agreement, expected future salary increase and a rate of 4.7% used to discount the future obligations, determined by reference to 10-years high quality corporate bonds in the euro area. Considering the fact that assumptions used in the calculation are not changing significantly in the individual year and that they remain inside the corridors set by the aforementioned standard, the decision was taken that the actuarial calculation is performed every five years.

Provisions for known risks relate to potential liabilities of the Bank towards creditors of several Savings and Loan Undertakings and to the potential liabilities streaming from off-balance sheet positions. For the latter, the provision amounting to EUR 64.7 million has been created in 2009. The provision relates to the price risk of invested assets, received as collateral for securities lent via agent banks.

Provisions for general risks

Taking into account the Bank's exposure to interest rate, exchange rate and price risks, provisions for future unrealised interest rate losses have been created in year 2007, amounting to EUR 15.3 million, and EUR 4.7 million in year 2008. In 2010, the Bank created additional general provisions amounting to EUR 33.1 million.

Provisions in respect of monetary policy operations

In accordance with Article 32.4 of the Statute, the provision against counterparty risks in monetary policy operations is allocated between the national central banks of participating Member States (NCBs) in proportion to their subscribed capital key shares in the ECB prevailing in the year when the defaults have occurred. In accordance with the general accounting principle of prudence, the Governing Council has reviewed the appropriateness of the volume of this provision and decided to reduce the provision from a total amount of EUR 4,011 million as at 31 December 2009 to an amount of EUR 2,207 million as at 31 December 2010. The Bank's share in this provision amounts to EUR 10.1 million (2009: EUR 18.4 million). The respective adjustments are reflected in the NCB's profit and loss accounts. In case of Bank of Slovenia the resulting income amounted to EUR 8.3 million in 2010 (see Profit and loss account item 5 'Net result of pooling of monetary income').

14. Revaluation accounts

The positive difference between the market value and the average acquisition costs in the case of gold holdings, net positions in each foreign currency and securities portfolio is shown in this balance sheet item.

In case of valuation of securities, gains of EUR 95.5 million arose from the valuation of EUR denominated portfolio (2009: EUR 120.3 million), EUR 8.9 million from the valuation of USD denominated assets (2009: EUR 8.9 million), EUR 4.9 million from AUD denominated securities portfolio (2009: EUR 4.9 million) and EUR 0.4 million from the GBP denominated portfolio (2009: EUR 2.5 million).

In case of foreign currency positions, gains of EUR 11.0 million arose from the valuation of USD position, EUR 5.6 million from the valuation of CHF position and EUR 3.2 million from the valuation of SDR position (2009: EUR 1.9 million from the valuation of CHF position).

In case of gold the acquisition cost is 1 ozf = EUR 482.688 (2009: EUR 482.688), comparing with market price at the end of 2010, which was EUR 1,055.418 per fine ounce of gold (2009: EUR 766.347). Market value of gold position exceeded its acquisition price and resulted in a revaluation gain amounting to EUR 58.6 million (2009: EUR 29.0 million).

	31 December 2010	31 December 2009
	000 EUR	000 EUR
Price effect	109,715	136,487
- securities in foreign currencies (asset items 2 and 3)	14,252	16,209
- securities in euro (asset items 4 and 7)	95,463	120,278
Exchange rate effect	19,743	1,859
Gold value effect	58,610	29,032
Total	188,068	167,378

15. Capital and reserves

In accordance with the Article 5 of the Bank of Slovenia Act, the capital of the Bank was created from the general reserves in the amount of EUR 8.3 million in year 2002. Banka Slovenije's initial capital may be increased by allocating of funds from the general reserves in an amount to be determined by the Governing Board.

The reserves of the Bank of Slovenia are composed of general reserves and special reserves. General reserves serve to cover general risks associated with the operations of the Bank of Slovenia. Special reserves serve to cover exchange rate and price risks. Special reserves are equal to the amount of unrealised income deriving from exchange rate and price changes until the end of 2006. Investment properties revaluation reserve are created out of the valuation gains arising from the appraisal of the investment properties in Austria, performed by the independent real estate assessor.

	31 December 2010	31 December 2009
	000 EUR	000 EUR
Composition of reserves:		
Initial capital of the Bank of Slovenia	8,346	8,346
General reserve	361,692	284,018
Special reserve for foreign exchange differences	380,714	380,714
Special reserve – price risk (gold)	43,236	43,236
Revaluation reserve	8,039	8,039
Total reserves	802,027	724,352

Notes to the off-balance-sheet items

Foreign currency swaps

As at 31 December 2010, the forward foreign currency position arising from EUR/foreign currency swap transactions amounts to EUR 365.6 million (2009: EUR 409.2 million).

In addition, off-balance sheet items include forward liabilities to the ECB and forward claims against Slovenian counterparties outstanding as at 31 December 2009, which arose in connection with the provision of Swiss franc funding to Slovenian counterparties. Swiss francs were provided by the Swiss National Bank to the ECB by means of a swap arrangement. The ECB simultaneously entered into swap transactions with NCBs that have adopted the euro, which used the resulting funds to conduct Swiss franc liquidity-providing operations with the Eurosystem counterparties against euro cash in the form of swap transactions. The swap transactions between the ECB and the NCBs resulted in intra-Eurosystem balances reported under 'Other claims within the Eurosystem (net)'. At the end of 2010, Bank has no such claims and liabilities.

The forward claims and forward liabilities in foreign currencies were revalued at the same exchange rates as those used for spot holdings in foreign currencies.

	31 December 2010		31 December 2009	
	000 Foreign currency	**000 EUR**	**000 Foreign currency**	**000 EUR**
Forward liabilities in AUD	114,800	87,393	189,400	118,316
Forward liabilities in GBP	15,500	18,008	41,000	46,166
Forward liabilities in USD	347,700	260,216	352,500	244,690
Total	-	**365,617**	-	**409,172**
Forward liabilities to ECB in CHF	-	-	1,510	1,018
Forward claims against Eurosystem counterparties in CHF	-	-	1,510	1,018

Securities lending

As at 31 December 2010, securities with a market value of EUR 650 million (31 December 2009: EUR 821 million) were lent under automated security lending contracts with the agents, which were, in case of collateral, reinvested into reverse repo transactions, prime asset backed securities, bank bonds and certificates of deposits.

Other off-balance-sheet items

The following other financial liabilities of the Bank were stated off-balance-sheet as at 31 December 2010:

- obligation under the IMF's statutes to provide currency on demand in exchange for SDRs up to the point at which the Bank's SDR holdings are three times as high as the amount it has received gratuitously from the IMF, which was equivalent to EUR 520.1 million as at 31 December 2010 (31 December 2009: EUR 489.3 million);

- a contingent liability of EUR 164.4 million, equivalent to the Bank's share of the maximum of EUR 50 billion reserve assets that the ECB may require the euro area NCBs to transfer under Article 30.1 ESCB Statute (31 December 2009: EUR 164.4 million);

- a future liability of EUR 11.0 million, which corresponds to the Bank's unpaid contribution to the ECB's capital[15] (see section on asset item 9 'Intra-Eurosystem claims) (31 December 2009: contingent liability EUR 16.4 million).

Notes to the profit and loss account

1. **Net interest income (expenditure)**

Interest income

Net interest income consists of interest income on foreign reserve assets and euro-denominated portfolio and interest income on euro-denominated claims. Euro-denominated claims include monetary policy instruments, foreign reserve assets transferred to the ECB and net claim arising from the allocation of banknotes within the Eurosystem.

[15] Decision of the European Central Bank of 13 December 2010 on the paying-up of the increase of the European Central Bank's capital by the national central banks of Member States whose currency is the euro (ECB/2010/27), OJ L 11, 15.01.2011, p. 54-55.

	31 December 2010	31 December 2009
	000 EUR	000 EUR
Interest income		
Gold	**146**	**212**
Current accounts and deposits	**1,693**	**5,500**
- In foreign currency	241	326
- In euro	1,452	5,174
Securities	**108,529**	**125,295**
- In foreign currency	16,741	22,470
- In euro	91,788	102,825
IMF	**786**	**333**
Monetary policy operations	**16,248**	**18,406**
- Main refinancing operation	54	1,499
- Longer-term refinancing operations	16,185	16,906
- Other refinancing operations	9	0
Intra Eurosystem claims	**17,744**	**19,169**
- Claims arising from the transfer of foreign reserves to the ECB	1,632	2,087
- Net claims related to the allocation of banknotes within the Eurosystem	16,111	17,082
Foreign currency swaps	**279**	**1,421**
Other interest income	**33**	**184**
Total	**145,458**	**170,519**

Interest expense

Interest expense arises from the liabilities in form of government accounts and deposits and monetary policy operations with the aim to absorb liquidity. The latest mainly concerns interest paid on banks' minimum reserves and overnight deposits. Interest expense also includes interest paid on TARGET2 balances.

	000 EUR	000 EUR
Interest expenditure		
Current accounts and deposits	**2,189**	**2,202**
- In foreign currency	180	130
- In euro	2,009	2,071
IMF	**635**	**178**
Monetary policy operations	**5,547**	**7,398**
- Minimum reserves	4,296	5,494
- Overnight deposits	935	1,793
- Fixed term deposits	316	110
Intra Eurosystem liabilities	**30,000**	**40,583**
- TARGET balances	30,000	40,583
Foreign currency swaps	**4,488**	**3,303**
Other interest expense	**4**	**16**
Total	**42,864**	**53,680**

2. Net result of financial operations, write-downs and risk provisions

The net income shown in sub-item 'Realised gains/losses arising from financial operations' arose from the sale of gold, currency positions and securities.

Write-downs of financial assets and positions reflect the decline in market prices of balance sheet items as at 31 December 2010 below the average cost of the respective currencies or securities. The valuation losses in 2010 occurred mostly in EUR denominated securities (the same as in 2009).

Transfer to provisions for special risks amounting to EUR 33.1 million represents the amount of provisions, created for potential losses from interest rate, price and exchange rate risks.

According to the Governing Board decision, additional provisions have been made for the certain legal claims pending, in the amount of EUR 0.5 million.

	31 December 2010	31 December 2009
	000 EUR	000 EUR
Realised gains/losses		
Gold	-	-
Currency position	3,038	1,560
Securities	28,169	61,227
Total	31,208	62,787
Write-downs		
Currency position	-476	-1,717
Securities	-58,611	-13,396
Total	-59,087	-15,113
Transfer to/from provisions for foreign exchange risks, price risks and other operational risks		
Provisions for specific risks	-535	-64,894
Provisions for general risks	-33,100	-
Total	-33,635	-64,894
Total	-61,514	-17,220

3. Net fee and commission income

Fees and commissions receivable mainly arise from payment and settlement service, supervisory and regulatory functions and security lending transactions. Fees and commissions are paid for the domestic and foreign bank's payment services and to the commercial banks for their readiness to provide liquidity loans to other banks.

4. Income from equity shares and participating interests

This item represents the Bank's dividends received on Bank's shares in the international financial institutions and the ECB.

Also included under this caption is the distribution of the ECB's income on euro banknotes (2009: EUR 3.7 million) (see 'Banknotes in circulation' in the notes on accounting policies). In 2010 the ECB's income on euro banknotes in circulation and on SMP securities was fully retained by the ECB in accordance with a decision of the Governing Council with respect to the establishment of a provision for foreign exchange rate, interest rate, credit and gold price risks. The retained amount not distributed to the Bank amounts to EUR 5.2 million.

5. Net result of pooling of monetary income

The monetary income of the Eurosystem national central banks is allocated in accordance with the decision taken by the Governing Council of the ECB[16]. The amount of each Eurosystem NCB's monetary income is determined by measuring the actual annual income that derives from the earmarkable assets held against its liability base.

Any interest paid on liabilities included within the liability base is to be deducted from the monetary income to be pooled by the NCB.

Where the value of a NCB's earmarkable assets exceeds or falls short of the value of its liability base, the difference shall be offset by applying to the value of the difference the latest available marginal rate for the Eurosystem's main refinancing operations. At the end of each financial year the total monetary income pooled by the Eurosystem is allocated among the NCBs according to the subscribed ECB capital key. The difference between the monetary income pooled and that reallocated to the individual NCB constitutes the net result arising from the calculation of monetary income recorded in the Profit and Loss account.

In the year 2010 the allocation of monetary income resulted in a net liability of EUR 0.2 million for the Bank (2009: net claim amounting to EUR 6.9 million). This net claim consists of the claim for year 2010, which represents the difference between the EUR 49.1 million (2009: EUR 46.8 million) of monetary income paid by the Bank into the common pool and the Bank's claim of EUR 49.3 million (2009: EUR 53.7 million) on the common pool, corresponding to the Bank's share in the ECB's paid-up capital, and of liabilities resulting from subsequent adjustment for years 2008 and 2009.

This item also includes the net result of the provisioning against counterparty risks in monetary policy operations of the Eurosystem amounting to an income of EUR 8.3 million (2009: income of EUR 7.9 million; see section on liability item L13 on provisions).

6. Other operating income

Other operating income includes income from non-bank services like rental income, income from confirmations issued, numismatics and other income.

7. Operating expenses

Staff costs

Staff costs include salaries and other staff costs together with the related taxes and contributions.

The Bank employed 420 employees as at 31 December 2010 (31 December 2009: 428 employees).

In accordance with the contract between the Bank and the Trade union from March 2002 Bank employees have been included into Voluntary supplementary pension insurance, which is defined as a contribution plan. Staff costs include contribution of the Bank for Voluntary supplementary pension insurance of EUR 0.5 million (2009: EUR 0.4 million).

[16] Decision of the European Central Bank of 25 November 2010 on the allocation of monetary income of the national central banks of member states whose currency is euro (ECB/2010/23), OJ L 35, 09.02.2011, p. 17-25.

In 2010 the remuneration of the Governing board members of the Bank was of EUR 0.7 million (2009: EUR 0.7 million).

Other operating expenses

This item consists mainly of expenses relating to the building and equipment maintenance, renting expenses, business travel and training costs, communication and energy costs, IT related expenses (software maintenance, system assistance), expenses for services outsourced, expenses for small goods and materials and other office expenses.

Depreciation of tangible and intangible fixed assets

Depreciation of buildings, furniture and office equipment, computer hardware and software was performed according to the adopted depreciation rates.

Banknote production services

Expenses for banknotes production services include mainly the expenses related to the production and transportation. The additional quantity of banknotes to be printed is determined on the basis of assessed needs for banknotes in circulation and for the maintenance of adequate volume of stock in the Eurosystem, distributed to individual NCB according to its capital key and denomination structure.

Other expenses

Other expenses consist mainly of contributions of the Bank, taxes and other operating expenses.

8. Profit for the year

According to the Accounting Guideline, to which the unrealised valuation losses shall be covered from the current financial result, whilst the unrealised valuation gains are transferred directly to revaluation accounts, the Bank shows the profit amounted to EUR 38.2 million (2009: EUR 103.6 million). In accordance with the second paragraph of the Article 50 of the Law on the Bank of Slovenia, 25% share of the financial result (EUR 9.5 million) will be transferred to the Republic of Slovenia budget. The remaining amount will be allocated to the Bank's general reserves.

5 APPENDICES

5.1 Publications and website

Title and basic information	Contents
Bilten **[Monthly Bulletin]** • monthly • in Slovene and English	Macroeconomic statistics with an emphasis on monetary statistics, exchange rates and economic relations with the rest of the world. Economic and financial developments; methodological appendix; review of Slovenian banks, calendar of data releases.
Letno poročilo **[Annual Report]** • annual (released in spring) • in Slovene and English	Report by the Bank of Slovenia to the National Assembly of the Republic of Slovenia. Description of economic developments, monetary policy, operations of banks and the Bank of Slovenia, and other activities of the Bank of Slovenia.
Neposredne naložbe **[Direct Investment]** • annual • in Slovene and English	Statistical review of direct and portfolio investment vis-à-vis Slovenia, both inward and outward (on an annual basis).
Finančni računi Slovenije **[Financial Accounts of Slovenia]** • annual • in Slovene and English	Comprehensive review of unconsolidated and consolidated sectors of the financial account of the Republic of Slovenia in an internationally comparable manner.
Prikazi in analize **[Surveys and Analyses]** • quarterly • in Slovene and English	Analytical and methodological presentations from macroeconomic and other areas.
Finančni trgi **[Financial Markets]** • quarterly	Statistical review of non-monetary financial intermediaries, the securities market and interest rates.
Poročilo o cenovni stabilnosti **[Price Stability Report]** • half-yearly • in Slovene and English	Publication focuses on projections of basic macroeconomic indicators for Slovenia for the next two years with accompanying risk factors. The publication also assesses movements in macroeconomic aggregates in the domestic and international economic environments with an emphasis on inflation trends. It illustrates movements in competitiveness indicators of the Slovenian economy and monitors country's fiscal position. It assesses the impact of financing conditions on the real sector with an overview of the main types of financing.
Poročilo o finančni stabilnosti **[Financial Stability Review]** • annual • in Slovene and English	The Financial Stability Review is intended primarily for the analytical monitoring of developments in the banking sector, and articles by experts on maintaining financial stability.
Website • index of Slovenian pages http://www.bsi.si/ ... ... /html/kazalo.html • index of English pages http://www.bsi.si/... ... /eng/index.html	Website of the Bank of Slovenia with information about the institution, banknotes and coins, laws and regulations governing the work of the central bank, and other useful information. Current data on exchange rates, interest rates and securities, and major publications available for download in electronic form.

5.2 Secondary legislation affecting banking supervision

January 2010	-	Regulation on the deposit guarantee scheme
	-	Guidelines for completing and submitting guaranteed deposit reports
	-	Regulation amending the regulation on the amounts of annual fees for supervision and fees for decisions regarding requests for the granting of authorisation
February 2010	-	Regulation amending the regulation on electronic money issuing companies
March 2010	-	Regulation amending the regulation on the calculation of the capital requirements for credit risk using an internal ratings-based approach for banks and savings banks
August 2010	-	Regulation amending the regulation on the recognition of external credit assessment institutions
September 2010	-	Regulation on the conditions to be met by credit intermediaries
	-	Regulation amending the regulation on reporting the effective interest rates of banks and savings banks in accordance with the consumer credit act
	-	Guidelines for implementing the regulation on the assessment of credit risk losses of banks and savings banks
October 2010	-	Regulation on the calculation of the capital of banks and savings banks
	-	Regulation on large exposures of banks and savings banks
	-	Regulation on the calculation of capital requirements for credit risk in securitisation and rules regarding the exposure of banks and savings banks to credit risk transfer
	-	Regulation amending the regulation on risk management and implementation of the internal capital adequacy assessment process for banks and savings banks
	-	Regulation amending the regulation on the calculation of capital requirements for credit risk using the standardised approach for banks and savings banks
	-	Regulation amending the regulation on the calculation of the capital requirements for credit risk using an internal ratings-based approach for banks and savings banks
	-	Regulation amending the regulation on credit protection
	-	Regulation amending the regulation on the calculation of capital requirements for market risks for banks and savings banks
	-	Regulation amending the regulation on the calculation of capital requirements for operational risk for banks and savings banks
	-	Regulation amending the regulation on disclosures by banks and savings banks
	-	Regulation amending the regulation on the reporting of capital and capital requirements for banks and savings banks
	-	Regulation amending the regulation on the reporting of certain facts and circumstances relating to banks and savings banks

December 2010	- Regulation on the deposit guarantee scheme - Regulation amending the regulation on the amounts of annual fees for supervision and fees for decisions regarding requests for the granting of authorisation - Regulation amending the regulation on the books accounts and annual reports of banks and savings banks - Regulation amending the regulation on the supervision of banks and savings banks on a consolidated basis - Regulation amending the regulation on the investments of banks and savings banks in qualifying holdings in entities in the non-financial sector - Regulation amending the regulation on the calculation of the capital of banks and savings banks - Regulation amending the regulation on the calculation of capital requirements for credit risk using a standardised approach for banks and savings banks

5.3 Glossary of selected terms

Money market – The market on which short-term (up to one year) securities are traded and short-term deposits are made.

Eonia (Euro OverNight Index Average) – The effective overnight reference rate for overnight, unsecured interbank lending in euro. It is calculated daily as the weighted average interest rate on lending by a pre-selected group of banks. The panel includes major banks operating in the euro interbank market.

ESCB – The European System of Central Banks comprises the European Central Bank (ECB) and the national central banks of EU Member States.

Euro area – The area encompassing the EU Member States that have adopted the euro as their currency in accordance with the Treaty and in which a single monetary policy is conducted under the responsibility of the Governing Council of the ECB.

Eurosystem – Comprises the European Central Bank and the national central banks of the euro area.

ECB key interest rate – The interest rate used by the Eurosystem to signal the monetary policy stance. It is the same as the main refinancing operation's minimum bid rate.

Covered bond – A bond issued by a bank and secured by the property of the issuer (e.g. mortgage loans). If the issuer is unable to repay a bond, the holder has a preferential right to a payout from the sale of said property.

Liquidity deficit – Sum of central bank's net autonomous liabilities and the reserve requirement.

Deposit facility – A standing facility of the Eurosystem that counterparties may use to make overnight deposits at a national central bank at an interest rate that is generally lower than the market interest rate (Eonia).

Marginal lending facility – A standing facility of the Eurosystem that counterparties may use to receive overnight credit from a national central bank at an interest rate that is usually higher than the market interest rate (Eonia).

National central bank – Any central bank in the euro area except the ECB. In Slovenia it is the Bank of Slovenia.

Benchmark allotment – The amount of an MRO allotment that enables banks to regularly meet their reserve requirement smoothly over the maintenance period.

Reserve requirement – The minimum prescribed amount of money that credit institutions (banks and savings banks) are obliged to maintain on their accounts at a central bank on average over the reserve maintenance period. The amount is calculated by multiplying the reserve base (i.e. selected liabilities in credit institutions' balance sheets) by the reserve ratio. The reserve ratio in the euro area is 2% for liabilities with a contractual maturity of up to two years, and 0% for liabilities with a maturity of more than two years and for those arising from repo transactions. Liabilities to the Eurosystem and other institutions subject to the minimum reserve system of the Eurosystem are not included in the base. The reserve maintenance period typically starts on the Wednesday following the meeting of the Governing Council of the ECB, when the latter makes decisions regarding the ECB's key interest rate, and ends on Tuesday prior to such Wednesday in the next month.

Standing facility – A central bank facility available at all times to counterparties at their own initiative. The Eurosystem offers two overnight standing facilities: the marginal lending facility and the deposit facility.

Full allotment – The allotment procedure in Eurosystem open market operations, where the Eurosystem allots the full amount to a bank at a tender, without regard to the total demand of all banks at that tender. It has been used since October 2008.

Reverse transaction – An operation whereby the national central bank simultaneously buys and sells (or vice-versa) financial assets under a repurchase agreement or conducts credit operations against collateral, with differing settlement dates. The opposite is an outright transaction comprising only one part (there is no reversing part), i.e. a national central bank buys or sells financial assets (typically securities) on the market.

Excess liquidity – The amount of the banking system's liquidity that exceeds the benchmark allotment amount.